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No. 89-

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1989

JAMES L. SHORES, JR., Executor of the Estate of Clarence E. Bishop, Jr., on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Town of Frisco City, Alabama,

Petitioner,

v.

JERALD H. SKLAR, et al.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1. Does a plaintiff who files an action alleging both individual claims and class claims under Rule 23, F.R.Civ.P. present two separate issues for judicial resolution, the claim on the merits and the claim that he is entitled to represent a class, so that in a case in which class certification is denied by the district court and the putative class representative accepts a Rule 68, F.R.Civ.P. offer of judgment on his individual claim, the necessary Article III requirements for a justiciable controversy exist with respect to an appeal by the putative class representative of the order denying class certification even though the putative class representative's claim on the merits has been resolved?

2. Does the acceptance of a Rule 68, F.R.Civ.P. offer of judgment in settlement of his individual claim by the putative class representative in a putative class action proceeding after the district court has denied class certification deprive the court of appeals of subject matter jurisdiction to hear a subsequent appeal by the putative class representative only of the denial of class certification?

3. Does Rule 23(e), F.R.Civ.P., requiring notice to all putative class members prior to dismissal or compromise of

class claims, apply in an action filed as a putative class action where the putative class representative accepts a Rule 68, F.R.Civ.P. offer of judgment after the district court denies class certification and the effect of the resulting resolution of the putative class representative's individual claim is held by the court of appeals to deprive the circuit court of subject matter jurisdiction to hear a subsequent appeal of the interlocutory order denying class certification, thus causing the loss of all class claims?

4. Is the *en banc* opinion of the circuit court of appeals in this case holding that a putative class representative who, after the district court refused to certify the class, accepted a Rule 68, F.R.Civ.P. offer of judgment in settlement of his individual claim without reserving the right to appeal the interlocutory order denying class certification, deprived the court of appeals of subject matter jurisdiction to hear the appeal of the denial of class certification, in conflict with the decisions of this Court in *United States Parole Commission v. Geraghty*, 445 U.S. 388, 100 S. Ct. 1202, 63 L. Ed. 2d 479 (1980) and *Deposit Guaranty National Bank v. Roper*, 445 U.S. 326, 100 S. Ct. 1166, 63 L. Ed. 2d 427 (1980)?

5. Does the opinion sought to be reviewed conflict with the opinion in *Love v. Turlington,* 733 F.2d 1562 (11th Cir. 1984), which stated the applicable law at the time the putative class representative accepted a Rule 68, F.R.Civ.P. offer of judgment in reliance on the holding in *Love* that the court of appeals would have subject matter jurisdiction of a subsequent timely filed appeal of the interlocutory order denying class certification, and, if so, can the putative class members be deprived of their claims without Rule 23(e), F.R. Civ.P. notice, even though the district court erred in refusing to certify the class solely because the reinterpretation of *Love* holds that the putative class representative's acceptance of the Rule 68 offer of judgment without a specific reservation of the right to pursue such an appeal deprived the court of appeals of subject matter jurisdiction of such appeal?

THE PARTIES BELOW

Petitioner

James L. Shores, Jr. as executor of the estate of Clarence E. Bishop on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Town of Frisco City, Alabama.

Respondents

Jerald H. Sklar, Allen Cox, Jr., Roane Waring, Jr., Erich W. James, Robert L. Cox, Lucas F. Allen, Fred L. Watson, Jr., a partnership engaged in the practice of law as Waring, Cox, James, Sklar and Allen, Cecil J. Lamberson, Jackson Municipals, Inc., a corporation Clarence Hamilton Investors Associates of American, Inc., a corporation, The Estate of George C. Rakerd Aza C. Candler, V. John H. Candler, Jr. Thomas E. Martin, Jr. Robin B. Page, Wilhelm Peppler, Joseph F. Savage, III, Jerry G. Yokley, Capell, Howard, Knabe & Cobbs, P.A. a professional association engaged in the practice of law, Montgomery, Alabama, First Alabama Bank of Phenix City

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Petitioner,

v.

JERALD H. SKLAR, et al.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

Petitioner, James L. Shores Jr., as executor of the estate of Clarence E. Bishop on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Town of Frisco City, Alabama, respectfully prays that a writ of certiorari issue to review the opinion of the United States Court of Appeals for the Eleventh Circuit

entered in the above-referenced matter on September 18, 1989.

OPINION BELOW

The opinion sought to be reviewed is *Shores v. Sklar*, 885 F.2d 760 (11th Cir. 1989) (App. A). Other opinions entered in this case are reproduced in the Appendix: August 2, 1977, opinion of United States District Court Judge Hancock dismissing the case (App. B); *Shores v. Sklar*, 610 F.2d 235 (5th Cir. 1980) (App. C); *Shores v. Sklar*, 617 F.2d 441 (5th Cir. 1980) (App. D); *Shores v. Sklar*, 647 F.2d 462 (5th Cir. 1981) (App. E); *Sklar v. Shores*, 459 U.S. 1102 (1983) (App. F); *Shores v. Sklar*, Civ A. 75-G-618-S (D.Ct. N.D. Ala. July 30, 1986) (App. G); *Shores v. Sklar*, 844 F.2d 1485 (11th Cir. 1988) (App. H); *Shores v. Sklar*, 855 F.2d 722 (11th Cir. 1988)(App. I).

JURISDICTION

This Court's jurisdiction is invoked under 28 *U.S.C.* § 1254(1).

STATUES AND REGULATIONS

Statutes: § 10(b), Securities Exchange Act of 1934, 15 *U.S.C.* § 78; (b) (App. J). Regulations: S.E.C. Rule 10b-5, as set out in 17 *C.F.R.* § 240.10b-5. (App. K).

STATEMENT OF THE CASE

A. Nature of the Case

This case began its long, tortured route through the judicial system over fourteen years ago. Clarence E. Bishop, Jr., individually and on behalf of persons who had purchased First Mortgage 8% Revenue Bonds issued by the Industrial Development Board of Frisco City, Alabama,[1] filed this case on May 16, 1975 in the United States District Court for the Northern District of Alabama alleging *inter alia* securities fraud. The district court entered an order two years later dismissing the case.[2] *Bishop v. Sklar*, No. 75-H-

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[1]These bonds were issued pursuant to the Wallace-Cater Act codified in *Code of Alabama* (1975), §11-54-80, *et seq.* The bonds were tax exempt. They were authorized so a local industrial development board organized under the Act could build a facility and then lease it to a commercial enterprise. The sole source for payment of interest and principal on such bonds is the rent payments made by the leasing commercial entity. The issuing local government has no liability on the bonds. The rental payments are calculated to amortize the principal and interest. The other sources of repayment are the assets of the lessee and any guarantors or the sale of the facility.

[2]The district court's order dismissing the case was based solely on certain of Mr. Bishop's answers to interrogatories in which he stated that he had never seen the offering circular issued in connection with the sale of the bonds and did not know that one existed. The district court held that these answers established a lack of reliance and thus a failure to state a claim under §10b or Rule 10b(5). The district court also refused to certify the class based on these answers to interrogatories.

618-S, Slip op. (N.D. Ala. Aug.2, 1977). (App. B).

An appeal was taken to the former Fifth Circuit. In the meantime, Bishop died. The case was revived in the name of his executor, James L. Shores. The former Fifth Circuit reversed the decision of the district court in the first of the many Shores' opinions. *Shores v. Sklar*, 610 F.2d 235 (5th Cir. 1980). (App. C). After granting rehearing *en banc*, [*Shores v. Sklar*, 617 F.2d 441 (5th Cir. 1980) (App. D)], the former Fifth Circuit again reversed the district court's order. *Shores v. Sklar*, 647 F.2d 462 (5th Cir. 1981). (App. E). This court denied the respondent's petition for writ of certiorari. *Sklar v. Shores*, 459 U.S. 1102 (1983). (App. F).

The case was remanded to the district court (Judge Hancock) on May 29, 1983. A motion to certify the case as a class action was filed by petitioner. Testimony was taken on this motion by Judge Hancock on April 15, August 29 and September 29, 1985. Judge Hancock then recused himself because his wife had bought some stock related to one of the respondents. The case was reassigned to Judge Guin. On July 30, 1986, without hearing any testimony, he denied class certification. Shores' individual claim was set for trial.

Shores v. Sklar, No. 75-G-618-S, Slip op. (N. D. Ala. July 30, 1986). (App. G).

The respondents then made petitioner a $20,600.00 offer of judgment pursuant to Rule 68, F.R. Civ. P. The offer was accepted. Petitioner refused to accept payment or to satisfy the resulting judgment, but timely filed an appeal of the interlocutory order denying class certification.

The respondents moved to dismiss the appeal claiming that acceptance by petitioner of the Rule 68 offer of judgment deprived the court of appeals of Article III jurisdiction.

On May 10, 1988, a divided panel of the Eleventh Circuit denied the respondents' motion to dismiss the appeal and reversed the district court's order refusing to certify the class. *Shores v. Sklar*, 844 F.2d 1485 (11th Cir. 1988). (App. H). The panel opinion was subsequently vacated on August 26, 1988, pursuant to an *en banc* request by the respondents. *Shores v. Sklar*, 855 F.2d 722 (11th Cir. 1988). (App. I). On September 18, 1989, the Eleventh Circuit entered an opinion dismissing the appeal on the sole ground that petitioner had failed to reserve the right to appeal the denial of class certification when he accepted the Rule 68 offer of judgment

on his individual claim. *Shores v. Sklar*, 885 F.2d 760 (11th Cir. 1989). (App. A).

B. Outline of the Facts

In 1972, ASECo requested the town of Frisco City, Alabama to establish an industrial development board and issue tax exempt Wallace-Cater Act bonds to finance a plant. Frisco City agreed. An industrial development board was established solely for that purpose. The development board signed a lease with ASECo on November 1, 1972. The underwriter retained Sklar as bond counsel. He prepared the lease, bond indenture, mortgage, closing papers and the offering circular for the bond issue. The offering circular contained many material misrepresentations and omitted material facts.

The bonds were sold in three increments. Bishop purchased three of the bonds in January 1973 for a total of $3,052.67, and one bond in February 1973 for $1,043.37. Bishop never read the offering circular. He never knew that one existed. The bonds were in default under the terms of the indenture even before the second and third increments were sold. ASECo, which actually had no assets, made two

rent payments before defaulting in April of 1974, and has made no further payments.[3]

On May 16, 1975, Bishop filed suit against the underwriter, lawyer, trustee and others. The principal of ASECo had been murdered in the meantime. The suit alleged that the respondents violated *inter alia*, § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (App. J) and SEC Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5. (App. K). The district court dismissed the case based on Bishop's lack of reliance on respondents' misrepresentations. (App. B)

A panel of the former Fifth Circuit reversed the district court. The respondents obtained *en banc* review. The court again reversed the district court, holding that the requisite element of reliance could be satisfied by proof that the plaintiff relied on the integrity of the market without a showing of direct reliance on specific misrepresentations by the respondents. Bishop asserted that the bonds were so

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[3] The trustee eventually foreclosed and sold the ASECo plant after this case was filed, paying 37% of the face amount of the bonds to the bondholders.

fraudulent that they were not entitled to be placed on the market at all and could not have been marketed but for the respondents' fraud. The court held that the element of reliance is presumed upon proof that the deception was so material that absent the deception the bonds could not have been marketed.

The respondents unsuccessfully petitioned this Court for a writ of certiorari, 459 U.S. 1102, (1983), (App. F). The case was remanded to the district court. The petitioner again moved for class certification. The district court denied the motion for class certification on July 30, 1986. The court found that petitioner had failed to prove (a) the existence of a class, (b) that the class was so numerous that joinder of all members was impracticable, (c) that petitioner's claims or defenses were typical of the claims and defenses of the class, or (d) that petitioner would adequately protect the interests of the class. (App. G)

The district court set petitioner's individual claim for trial in January of 1987. The district court simultaneously held that the petitioner could not introduce into evidence the answers to interrogatories made by Bishop before his

death, though these same answers had been used by Judge Hancock as the sole evidence to dismiss the case. Bishop had never been deposed. The district court specifically ruled that the petitioner was foreclosed from proving the circumstances of the purchase by Mr. Bishop. (App. G, pp. 15-16).

On November 25, 1986, the respondents made an offer of judgment pursuant to F.R.Civ.P. 68 to the petitioner in the amount of $20,600.00. The petitioner accepted this offer. Final judgment was entered in favor of the petitioner on November 29, 1986. [4]

[4] The petitioner's claim was thus set up to be "picked off." *Deposit Guaranty National Bank v. Roper*, 445 U.S. 326, 100 S.Ct. 1166, 63 L.Ed.2d 427 (1980). Refusal of the Rule 68 offer of judgment would inevitably result in a judgment adverse to the petitioner given the stated intention of the district court to exclude from evidence Bishop's answers to interrogatories and the specific finding that petitioner could not prove the circumstances of Bishop's purchase. The ruling of the district court on this point was critical since, according to the subsequent panel opinion, the circumstances of particular purchases by class members were not material as reliance on the market was presumed because of the degree of fraud alleged. (App. H, p. 21) Nevertheless, under the existing ruling of the district court the result of refusing the offer could only be the award of substantial costs against the petitioner. The only reasonable course for petitioner in view of the cases cited below, including *Love v. Turlington*, 733 F.2d 1562 (11th Cir. 1984), was to accept the Rule 68 offer of judgment for his individual claim and then appeal the collateral ruling denying class certification. The petitioner subsequently attempted to use the amount of the offer of judgment to establish the standard for recovery due each of the putative class members.

On December 22, 1986, the petitioner filed a notice of appeal from the order denying class certification. Respondents moved to dismiss for lack of jurisdiction. They argued that the petitioner's acceptance of the offer of judgment eliminated the case or controversy necessary for Article III jurisdiction.

On May 10, 1988, a divided panel of the Eleventh Circuit denied the respondents' motion to dismiss the appeal of the denial of class certification and reversed the district court's denial of class certification, citing *Love v. Turlington*, 733 F.2d 1562 (11th Cir. 1984) and *Deposit Guaranty National Bank v. Roper*, 445 U.S. 326, 100 S. Ct. 1166, 63 L. Ed. 2d 427 (1980).[5] The court discussed the decisions of this Court in *Roper* and in *United States Parole Commission v. Geraghty*, 445 U.S. 388, 100 S. Ct. 1202, 63 L. Ed. 2d 479 (1980), concluding that *Geraghty*, "left open whether a plaintiff who settles its individual claim after denial of class certification

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[5] The panel opinion stated that, "In a line of cases beginning with [*Roper*], the Supreme Court and this court have held that a named plaintiff may, after final judgment, appeal a district court order denying class certification even in some circumstances where the named plaintiff might be unable to appeal the final judgment itself." (App. H, p.10).

may appeal the adverse ruling." (App. H, p.12) The court held that in *Love v. Turlington*, 733 F.2d 1562 (11th Cir. 1981), "This court encountered precisely that situation..." and, "Finding 'no meaningful distinction between the settlement of the claim here at issue and the expiration of the claim in *Geraghty*,' this court held that the class certification issue continued to be a dispute capable of judicial resolution on appeal."[6] (844 F.2d at 1490). (App. H, pp. 12-13).

The respondents sought and obtained *en banc* reversal of the panel opinion. The court held that because of the "well- established principle that all interlocutory orders are merged into the final judgment [citation omitted] interlocutory orders denying class certification become part of the final judgment for purposes of appeal. [citation omitted].

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[6] The respondents attempted below to distinguish the *Love* case on the basis that the appellees in that case specifically reserved their right to appeal whereas the petitioner had not done so. The panel opinion rejected the relevance of this "distinction," holding, "We cannot agree that *Love* will bear this interpretation. It is true that in *Love* the defendants expressly agreed not to contest the appealability of the certification order. The *Love* panel considered the agreement irrelevant to the jurisdictional inquiry, however, due to the established principle that federal subject matter jurisdiction cannot be created by agreement of the parties." (844 F.2d at 1490). (App. H, p. 13).

Accordingly, in the absence of qualification, consent to judgment constitutes consent to the interlocutory order denying class certification."[7] (885 F.2d at 763). (App. A, pp. 8-10).

The court then held that petitioner had consented to judgment in the "entire action," including the class claims, and dismissed the appeal. (App. A., p. 12)

REASONS FOR GRANTING THE WRIT

I. The Opinion Sought To Be Reviewed Is Contrary To A Well Established Line of Cases Decided By This Court

A line of decisions of this Court hold that federal appellate courts have subject matter jurisdiction to hear appeals

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[7] The *en banc* opinion held that in *Love* the court had made a distinction between the plaintiff reserving the right to appeal and the agreement between the plaintiff and defendant that the defendant would not contest the appealability of the interlocutory order denying class certification after the settlement. The alleged distinction is that the agreement was irrelevant, but the reservation of the right to appeal was dispositive of the right to appeal. Since petitioner did not reserve the right to appeal when he accepted the Rule 68 offer of judgment, the court held that the appeal of the interlocutory order denying class certification must be dismissed. This new and previously unsupported rule is legally wrong because, (1) it makes subject matter jurisdiction depend on the conduct of the parties, and (2) it allows the putative class representative to extinguish the rights of the putative class without notice to the class as required by Rule 23(e), F.R. Civ.P.

by named plaintiffs in putative class actions of interlocutory orders denying class certification even though the individual claims of the named plaintiffs have been resolved, by settlement or otherwise. The first cases in this line hold that this rule applies where the class has already been certified at the time the named plaintiff's claim is resolved. Subsequent decisions have extended the rule to cases in which the class has not been certified or where certification has been denied prior to the resolution of the named plaintiff's claim.

These cases begin with *Sosna v. Iowa*, 419 U. S. 393, 95 S. Ct. 553, 42 L. Ed. 2d 532 (1975). The petitioner there moved to Iowa and filed a divorce petition. The action was dismissed because she did not meet the residency requirement. The petitioner then brought a class action in federal court seeking injunctive and declaratory relief claiming that the Iowa residency requirement violated the Federal Constitution. The court granted class certification, but upheld the residency requirement. The petitioner appealed. Meanwhile, she moved to another state and obtained a divorce. The respondent alleged that this mooted the petitioner's individual claim and that the courts had no

jurisdiction to hear her appeal on behalf of the class of the decision upholding the residency requirement. This Court rejected that argument and held that the mootness of the individual claim did not affect the jurisdiction of the court to hear the appeal where the class had been certified **before** the individual claim was resolved.[8]

In *Franks v. Bowman Transportation Company*, 424 U.S. 747, 96 S. Ct. 1251, 47 L. Ed. 2d 444 (1976), this Court allowed the appeal of a **certified** class action case to go forward even where the class representative's individual claim had been resolved.

Beginning with the case of *United States Parole Commission v. Geraghty*, 445 U.S. 388, 100 S. Ct. 1202, 63 L. Ed. 2d 479 (1980), the rule of *Sosna* and *Franks* was applied where the class certification was either not ruled on or was

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[8] This Court stated:

> "If appellant had sued only on her own behalf, both the fact that she now satisfies the one year residency requirement and the fact that she has obtained a divorce elsewhere would make this case moot and require dismissal. [citations omitted] But appellant brought this case as a class action and sought to litigate the constitutionality of the durational residency requirement in a representative capacity. When the District Court certified the propriety of the class action, the class of unnamed persons described in the certification acquired a legal status separate from the interest asserted by appellant." (419 U.S. at 399)

denied prior to the resolution of the claims of the named plaintiff. In *Geraghty*, the respondent brought an action individually and on behalf of all other prisoners similarly situated challenging parole release guidelines. The district court **denied** class certification and granted summary judgment for the Parole Commission on the merits. The respondent appealed successfully on both issues to the court of appeals, but while the appeal was pending he was released from prison. The petitioner claimed this resolved respondents' individual claims and mooted the appeal of the interlocutory order denying class certification. The court of appeals and this Court rejected this contention. This Court held that an action brought on behalf of a class does not become moot upon expiration of the named plaintiff's substantive claim, even where class certification has been **denied**, because the putative class representative retains a sufficient "personal stake" in obtaining class certification to satisfy Article III "case or controversy" standards.[9]

[9] This Court reasoned that a plaintiff who brings a putative class action presents **two separate issues** - the claim on the merits and the claim he is entitled to represent a class. Consequently, the necessary Article III requirements for a justiciable controversy exist with respect to the appeal of the order denying class certification even though the named plaintiff's claim on the merits has been resolved and class certification has been denied.

The acceptance of the Rule 68, F.R.Civ.P. offer of judgment by the petitioner in this case was involuntary in the same sense as was the judgment in favor of the named plaintiffs in *Deposit Guaranty National Bank v. Roper,* 445 U.S. 326, 100 S. Ct. 1166, 63 L. Ed. 2d 427 (1980).[10] The Roper opinion was issued on the same day as the *Geraghty* opinion. *Roper* takes *Geraghty* and the rules set out in *Sosna* and *Franks* to their logical conclusion by holding that regardless of the basis of the resolution of the named plaintiff's claim, it constitutes a resolution of only *one* of the *two* issues in the case, and jurisdiction to hear the appeal of the denial of the class certification survives such individual claim resolution.

In *Roper,* the respondents were holders of credit cards issued by the petitioner bank who brought suit claiming

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[10] Even though petitioner's acceptance of the Rule 68 offer of judgment was involuntary in the correct sense of that term in the context of this case, the decisive principle of law applicable to this case should not turn on the voluntary or involuntary nature of the resolution of the named plaintiff's claim. The correct principle is that the putative class representative represents two claims, his and that of the class, and resolution of his claim cannot extinguish that of the class, particularly in the absence of compliance with Rule 23(e), F.R. Civ. P. *Geraghty*; *Love v. Turlington*, *supra*; *Glidden v. Chromalloy American Corporation*, 808 F.2d 621 (7th Cir. 1986).

that the finance charges on the credit cards exceeded the maximum allowable under Mississippi law. If true, the petitioner was responsible under Mississippi law for twice the amount of the excess interest. The respondents brought the action individually and seeking certification for a class of credit card holders.

The district court denied the respondents' motion to certify the class and certified the denial for interlocutory appeal under 28 U.S.C. § 1292(b), which the Fifth Circuit denied. The petitioner then offered to pay the respondents all damages they could possibly recover on their individual claims. The respondents refused. Whereupon, the district court, over the objections of respondents, entered judgment in favor of the individual respondents for the maximum amount that they could recover. The respondents appealed seeking review of the denial of class certification.

The petitioner moved to dismiss the appeal claiming that there was no jurisdiction to hear the appeal since the case had been mooted by the entry of judgment in respondents' favor. The court of appeals rejected this argument, accepted the appeal, reviewed the district court's ruling

denying class certification and ordered the class certified.

This Court held that the critical inquiry in the case, ". . . is whether respondents' individual and private case or controversy became moot by reason of petitioner's tender or the entry of judgment in respondents' favor." (445 U.S. at 332). This Court held that the court of appeals had jurisdiction of an appeal of the interlocutory denial of class certification despite the entry of a final judgment completely resolving the individual claims of the putative class representatives.[11]

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[11] This Court stated the applicable rule as follows:

> "We view the denial of class certification as an example of a procedural ruling, collateral to the merits of a litigation, that is appealable after the entry of final judgment. The denial of class certification stands **as an adjudication of one of the issues** litigated." (Emphasis supplied)
>
> ***
>
> "A district court's ruling on the certification issue is often the most significant decision rendered in these class-action proceedings . To deny the right to appeal simply because the defendant has sought to 'buy off' the individual private claims of the named plaintiffs would be contrary to sound judicial administration. Requiring multiple plaintiffs to bring separate actions, which effectively could be 'picked off' by a defendant's tender of judgment before an affirmative ruling on class certification could be obtained, obviously would frustrate the objectives of class actions; moreover, it would invite waste of judicial resources by stimulating successive suits brought by others claiming aggrievement." (Footnote omitted) (445 U. S . at 336, 339)

Moreover, an offer of judgment under Rule 68, F.R.Civ.P., and the acceptance thereof by the plaintiff in the class action context contains definite elements of coercion and is not a truly voluntary settlement. In *Marek v . Chesny*, 473 U. S. 1, 105 S. Ct. 3012, 87 L. Ed. 2d 1 (1985), this Court explained the meaning of Rule 68:

> "Rule 68 provides that if a timely pretrial offer of settlement is not accepted and 'the judgment finally obtained by the offeree is not more favorable than the offer, the **offeree must pay the costs incurred after the making of the offer**.' Fed Rule Civ Proc 68 (emphasis added). The plain purpose of Rule 68 is to encourage settlement and avoid litigation . Advisory Committee Note on Rules of Civil Procedure, Report of Proposed Amendments, 5 FRD 433, 483 n 1 (1946); [USCS Court Rules, F.R. Civ.P., Note following Rule 68]; Delta Air Lines, Inc. v. August, 450 U.S. 346, 352, 67 L. Ed. 2d 287, 101 S. Ct. 1146 (1981). The Rule prompts both parties to a suit to evaluate the risks and costs of litigation, and to balance them against the likelihood of success upon trial on the merits." (473 U.S. at 4-5)

A proposed amendment to Rule 68 would have added the following paragraph:

> "This rule shall not apply to class or derivative actions under Rule 23, 23.1, and 23.2." Preliminary Draft of Proposed Amendments to the Federal Rules of Civil Procedure, 102

F.R.D 425, 433 (1984).

The "Committee Notes" state:

> ...**the offeree's rejection would burden a named representative-offeree with the risk of exposure to potentially heavy liability that could not be recouped from unnamed class members.** The latter prospect, moreover, could lead to a **conflict of interest** between the named representative and other members of the class. (citations omitted) (Emphasis added) 102 F.R.D. at 436.

This proposed amendment to Rule 68 was not adopted, but the rationale for it supports the petitioner's argument concerning the coercive nature of a Rule 68 offer of judgment in the class action context.[12]

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[12] In *Marek v. Chesney, supra*, Justices Brennan, Marshall and Blackmun dissented and pointed out that: "Now that the Rule [68] has been extended to many attorney's fee provisions, these difficulties [intimidation of class representatives] can be expected to create substantial problems in administering class actions. [cite omitted] Rule 68 makes no distinctions between individual and class actions. [quoting advisory committee report above in text]...Moreover, Rule 23(e) requires the court's approval before a class action is compromised; the Rule protects class members from unjust or unfair settlements affecting their rights by representatives who lose interest or are able to secure satisfaction of their individual claims by compromise." [cite omitted] Yet Rule 68 does not mesh with such careful supervision. Its plain language requires simply that upon the plaintiff's acceptance the clerk *shall* enter judgment.[court's emphasis] In addition, Rule 68 sets a nondiscretionary 10-day limit on the plaintiff's power of acceptance-a virtually impossible amount of time in many cases to consider the likely merits of complex claims of relief, give notice to class members, and secure the court's approval." (473 U.S. at 33, n.49).

II. Rule 23(e), F.R. Civ. P., Required NoticeTo Putative Class members And An Opportunity To Object Before Class Claims Can Be Dismissed Or Compromised

Rule 23(e), F. R. Civ. P., states, "A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs."

Wright, Miller & Kane state in their treatise on the Federal Rules of Civil Procedure that, "The purpose of subdivision (e) is to protect the nonparty members of the class from unjust or unfair settlements affecting their rights when the representatives become fainthearted before the action is adjudicated or are able to secure satisfaction of their individual claims by a compromise."[13]

The cases suggest that this section should be applied to dismissal or compromises of putative class actions even

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[13] Wright, Miller & Kane, *Federal Practice and Procedure,* §1797, Volume 7B, page 340.

prior to a ruling on class certification.[14] What about a situation such as the instant one where the court of appeals has determined that the district judge improperly refused to certify the class, **but** that the class claims have been lost solely because subsequent to the denial of class certification a Rule 68 offer of judgment was accepted by the named plaintiff and putative class representative? Did the district court have a duty to give notice to the class that the acceptance of the Rule 68 offer of judgment by the class representative would extinguish the class claims even if the denial of certification was reversed?

In *McArthur v. Southern Airways, Inc.*, 556 F.2d 298 (5th Cir. 1977), *withdrawn on other grounds*, 569 F.2d 276 (5th Cir. 1978), *cert. denied* by 416 U.S. 993 (1974), the court held that Rule 23(e) applied where the plaintiffs after filing an action including individual and class claims made a favorable settlement of their individual claims and dis-

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[14] Wright, Miller & Kane, *Federal Practice and Procedure*, §1797, Volume 7B, page 347, "Thus, courts generally have agreed that actions filed as class suits are within the scope of Rule 23(e) even though they have not been formally certified at the time a settlement is reached."

missed the class claims under Rule 15(a), F.R. Civ.P., as part of the settlement. The district court held that prior to the defendants in a putative class action filing an answer and prior to the court's certification of the case as a class action, the putative class representatives could dismiss the class claims without complying with Rule 23(e), particularly where the district court found that the numerosity requirement for class certification under Rule 23(a)(1) had not been satisfied. (556 F.2d at 300-301).

The former Fifth Circuit reversed and remanded because there was no compliance with Rule 23(e), stating:

> Yet this settlement, which sacrifices the claims of absentee class members, enriches the class representatives and could ultimately prejudice the right of absent class members to assert their separate claims, provides a classic example of what rule 23(e) is designed to prevent. Because rule 15(a) should not be utilized in an attempt to circumvent the mandatory notice requirements of rule 23(e), we hold that the district court committed error in permitting plaintiffs to delete their class claims under rule 15(a) and proceed to settlement without first providing the absentee class members with notice of the proposed dismissal. (556 F.2d at 303).[15]

[15] This decision of the former Fifth Circuit is binding on the Eleventh Circuit under the holding in *Bonner v. City of Prichard*, 661 F.2d 1206 (11th Cir. 1981).

In *Glidden v. Chromalloy American Corporation*, 808 F.2d 621 (7th Cir. 1986), the plaintiff brought an action as a putative Rule 23(b)(3) class action. While the class certification motion was pending, the district court granted summary judgment for the defendant and deliberately withheld decision on class certification. The district court tried to carve up the case by ruling on the merits, allowing an appeal and withholding a class certification ruling.

The circuit court dismissed the plaintiffs' appeal of the summary judgment as not final because of the pendency of the class certification question. The plaintiff tried to dismiss the class claims without compliance with Rule 23(e) so the ruling would be a final judgment and appealable. The circuit court rejected the argument that Rule 23(e) "does not come into play until after a certification". (808 F.2d at 625-626). The court held:

> When notice would be a fruitless yet costly gesture, Rule 23(e) - read in light of Rule 1 - does not compel the parties to incur pointless expense. Excusing notice in a settled case should be rare, because as [*Simer v. Rios*, 661 F.2d 655, (7th Cir. 1981), *cert. denied*, 456 U.S. 917, 102 S.Ct. 1773, 72 L. Ed. 2d 177

> (1982),] observes the due process clause also is in play. Notice may be dispensed with more freely when the class claims are being dismissed. But *Simer* does not discuss the application of Rule 23(e) to dismissals or the extent to which the district court's approval is required. We conclude that what may not be dispensed with is the district court's approval of the elimination of an uncertified class claim. (808 F.2d at 627-628).

In *Diaz v. Trust Territory of Pacific Islands*, 876 F.2d 1401 (9th Cir. 1989), "The principal question on this appeal is whether the trial judge properly dismissed the class claims without notice to the class or inquiry into possible prejudice." (876 F.2d at 1403).

After filing a putative class action in addition to their individual claims, the plaintiffs realized the high cost of prosecuting the class claims and dismissed the class claims with the permission of the district court, without compliance with Rule 23(e).

The circuit court held that one of the reasons for requiring notice of dismissal of a class action is that it "protects the class from prejudice it would otherwise suffer if class members have refrained from filing suit because of knowledge of the pending class action." (876 F.2d at 1409). The Ninth Circuit concluded that even though absent class

members could still intervene in the action,

> In this case, the likelihood that members of the class had knowledge of the litigation, and the short time before expiration of the statute of limitations made prejudice likely. Given the possibility of prejudice from the November 15, 1985, dismissal of all claims by non-CNMI employees, the district court erred in not requiring notice to the non-CNMI class. (876 F.2d at 1411).

While none of these cases involve a situation in which the district court denied class certification before the resolution of the named plaintiff's individual claim, the rule of law ultimately imposed by the *en banc* Eleventh Circuit opinion in this case required dismissal of the class claims. The panel opinion which reversed the district court denial of class certification made it clear that the district court erred in denying class certification. (App. H, pp. 20-30). The district court was certainly aware of the effect of both the 1977 and 1986 opinions denying class certification on the rights of the absent class members.[16] The resulting preju-

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[16] In the 1977 opinion the district court stated:

> "Accordingly, the order to be entered will expressly authorize any putative class member, within six months after the entry of such order, to petition the court to intervene in this action to

dice to the absent class members is clear and could have been avoided by the use of Rule 23(e). The purpose and spirit of Rule 23(e) applies in this instance.

The only judgment to which the petitioner could legally have consented in this instant case in the absence of a Rule 23(e) compliance procedure was the judgment entered by the district court as to petitioner's individual claim. The petitioner cannot be required to "reserve" the right to appeal the denial of class certification as a jurisdictional requirement of a subsequent appeal since, in the absence of compliance with Rule 23(e), the right to such an appeal was "reserved" as a matter of law. Otherwise, the district court was derelict in its duty when it failed to follow the mandate

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> pursue his *individual* claim. Jurisdiction will be retained for the limited purpose of considering such a petition, and where the petitioner satisfies the court that he failed to pursue his individual claim in reliance upon this action being pursued for his benefit, the intervention will be allowed as if it had preceded the Rule 23(c) determination." (App. B, p.18).

In the 1986 opinion the district court acknowledged that he knew other class members may have been unaware of the pending loss of their claims, "The court is further of the opinion that Shores would not be an appropriate class representative. No one else having come forward as a potential party-class representative, class certification will be denied." (App.G, p. 7-8).

of Rule 23(e). The petitioner was legally incapable of consenting to any judgment which *extinguished* the claims of the class.

III. The Eleventh Circuit Changed The Law Of The Circuit After The Facts Of This Case Arose

In *Love v. Turlington*, 733 F.2d 1562 (11th Cir. 1984), the plaintiff appealed the district court's denial of class certification in a case which challenged the constitutionality of state student assessment tests on the basis that the tests were racially discriminatory. After the district court denied class certification, the plaintiff reached a negotiated consent settlement with the defendants as to her individual claim. A final judgment was entered. A condition of the settlement was that the defendants agreed not to contest the appealability of the denial of the class certification order. The Eleventh Circuit rejected the notion that this agreement had any effect on its jurisdiction to hear the appeal, holding that:

> It is an established principle of law that subject matter jurisdiction cannot be created or waived by agreement of the parties [citations omitted] and that lack of jurisdiction may be raised at any point in a proceeding by either party, or by the court itself upon

its own motion. 733 F.2d at 1564.

Love was the law in the Eleventh Circuit at the time the petitioner made the decision to accept the Rule 68 offer of judgment. The case clearly held that the court had jurisdiction to hear an appeal of an interlocutory order denying class certification after the individual claim of the named plaintiff was settled.[17]

The petitioner relied on the holding in *Love*, as well as the above referenced line of cases decided by this court, in accepting the Rule 68 offer. Under the *Love* holding, resolution of the petitioner's individual claim would not

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[17] The fact that *Love* is a mere extension of this Court's decisions on this point is clear from the *Love* opinion:

> "The Supreme Court has recognized that a class action plaintiff presents **two separate issues for judicial resolution**: the claim on the merits, and the claim that he is entitled to represent a class. *Geraghty*, 445 U.S. at 402, 100 S.Ct. at 1211. Application of the personal-stake requirement to a procedural claim such as the right to represent a class **is different** from application of the requirement to substantive claims... Finding **no meaningful distinction** between the **settlement** of the claim here at issue and the **expiration** of the claim in *Geraghty* for purposes of the ability of the named plaintiff to pursue an appeal of the denial of certification, we hold that a dispute capable of judicial resolution continues to exist with regard to the class certification issue in this case." (Emphasis supplied) 733 F.2d at 1565.

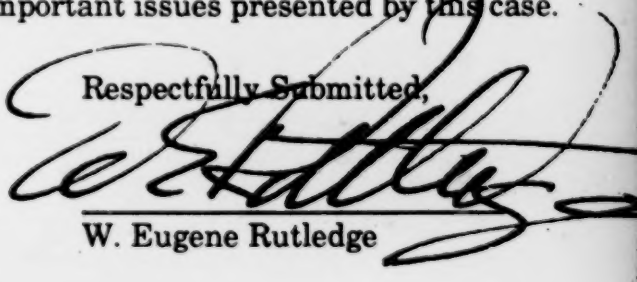
mean the loss of subject matter jurisdiction of a subsequent appeal of the denial of class certification. The Eleventh Circuit panel certainly agreed with the petitioner's interpretation of *Love*. (App. H). The claims of the plaintiff class should not be lost because the Eleventh Circuit decided after the facts arose to change its law.

Moreover, if the Eleventh Circuit's reinterpretation of *Love* and the consequent rule of law that reinterpretation establishes is allowed to stand, the coercive effect of Rule 68 offers of judgment in class actions will be destructive of the class action concept.

CONCLUSION

The petition for a writ of certiorari should be granted to resolve the important issues presented by this case.

Respectfully Submitted,



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APPENDIX

APPENDIX A

James L. SHORES, Jr., Executor of the Estate of Clarence E. Bishop, Jr., on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Industrial Board of the Town of Frisco City, Alabama,
Plaintiff-Appellant,

Jerald H. SKLAR, et al.,
Defendants-Appellees.

No. 86-7898.

United States Court of Appeals,
Eleventh Circuit.

Sept. 18, 1989.

Appeal from the United States District Court for the Northern District of Alabama.

Before RONEY, Chief Judge, TJOFLAT, HILL, FAY, KRAVITCH, JOHNSON, HATCHETT, ANDERSON CLARK, and COX, Circuit Judges * .

ANDERSON, Circuit Judge, with whom RONEY, Chief

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* Judges Vance and Edmondson are recused and did not participate in this decision.

Judge, and TJOFLAT, HILL, FAY and COX, Circuit Judges, concur:

[1] James L. Shores, Jr. appeals from the district court's denial of his motion to certify a class. Because we find that Shores' unqualified consent to entry of judgment in this action waived his right to appeal, the appeal is dismissed.[1]

I. FACTS

This securities fraud action commenced over thirteen years ago. On May 16, 1975 Clarence E. Bishop, Jr. filed a summons and complaint, individually and on behalf of all other persons who had purchased First Mortgage Revenue Bonds issued by the Industrial Development Board of Frisco City, Alabama. The complaint alleged that appellee Jerald Sklar (bond counsel), the Phenix National Bank (trustee of

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[1] With respect to the appeal by Habshey, who moved to intervene in the district court, we reinstate Part II.B. of the panel opinion. 844F.2d at 1491. We agree with the panel that Habshey's appeal was untimely. We also note Habshey's apparent abandonment of his appeal in that no argument on his behalf has been made to the en banc court.

the bond proceeds), and numerous others had issued a materially misleading offering circular and conspired to defraud purchasers, in violation of section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and the Securities and Exchange Commission's Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5.

In August 1977, the district court entered summary judgment for the defendants on Bishop's individual claims based on his admission that he had not read and relied on the circular. The court also denied certification of the class, finding an absence of typicality and adequate representation, and an insufficient basis for concluding that common questions of fact predominated. *Bishop v. Sklar,* No. 75-H-618-S, slip op. (N.D. Ala. Aug. 2, 1977).

On appeal by Shores, executor of Bishop's estate,[2] the former Fifth Circuit, sitting en banc, reversed, holding

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[2] The district court substituted Shores as party plaintiff after Bishop died.

that, under a version of the "fraud on the market" theory of recovery under Rule 10b-5, plaintiff's allegations were sufficient to withstand a motion to dismiss. *Shores v. Sklar*, 647 F.2d 462 (5th Cir.1981) (en banc), *cert. denied*, 459 U.S. 1102, 103 S.Ct. 722, 74 L.Ed.2d 949 (1983) *(Shores I)*. The court also instructed the district court to "reconsider the maintainability of this action as a class action as to members of a properly defined class of Bond purchasers who did not so rely." 647 F.2d at 472.

In July 1986, the district court on remand again denied class certification, finding no identifiable class, no adequate class representative, and an absence of numerosity and typicality. The court also set Shores' individual case for trial. *Shores v. Sklar*, No. 75-G-618-S, slip op. 1986 WL 9810 (N.D.Ala. July 30, 1986). In November 1986, certain of the defendants served upon Shores' counsel an offer, tendered in accordance with Fed.R.Civ.P. 68, "to allow judgment to be taken against them ... in this action, in the amount" of $20,600, and costs. Shortly thereafter Shores filed with the court notice of his acceptance of the defen-

dants' offer. On November 25, the court issued an order entering judgment in Shores' favor pursuant to the terms of the offer and acceptance.[3]

Following final judgment, Shores timely filed a notice of appeal from the July 1986 order denying class certification. A divided panel of this court reversed. *Shores v. Sklar*, 844 F.2d 1485 (11th Cir.1988) *(Shores II)*. A petition for rehearing was subsequently granted, vacating the panel opinion. 855 F.2d 722 (11th Cir.1988). We now hold that appellant's consent to an entry of judgment, given without reservation of a right to appeal, bars a subsequent appeal of the order denying class certification.[4]

II. DISCUSSION

[2] Shores argues that he settled only his individual

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[3] By agreement of the parties, the claims against the three remaining defendants - Wilhelm Peppler, Joseph Savage, and the Estate of George Rakerd - were dismissed with prejudice.

[4] Because we hold that the instant appeal is barred, we do not reach the other issues addressed in Shores *II* and discussed by the parties in their briefs.

claims, and that his claims on behalf of the putative class were unaffected by the district court's entry of judgment pursuant to the terms of the parties' settlement. Shores now seeks to appeal from the district court order refusing to certify the class. We find, however, that because he consented to the entry of judgment without reserving his right to appeal any portion thereof, Shores has waived his right to appeal the denial of class certification.

[3] The law is clear that consent to entry of judgment without reservation of the right to appeal a particular claim bars an appeal:

> Where the parties have agreed to entry of an order or judgment without any reservation relevant to the issue sought to be appealed, one party may not later seek to upset the judgment, unless lack of "actual consent" or a failure of subject matter jurisdiction is alleged.

Dorse v. Armstrong World Industries, Inc., 798 F.2d 1372, 1375 (11th Cir.1986). *See White v. C.I.R.*, 776 F.2d 976 (11th

Cir.1985) (party who consents to entry of judgment waives his right to appeal from it); *cf. Haitian Refugee Center v. Civiletti,* 614 F.2d 92 (5th Cir.1980) (party cannot appeal from an injunction to which he has agreed).

There is no contention that the settlement here was flawed by either a lack of "actual consent" or an absence of subject matter jurisdiction. Rather, Shores contends that the settlement and consent to entry of judgment resolved only his individual claims. Shores is correct that his individual claims and the claims on behalf of the putative class are distinct.[5] However, both sets of claims were brought by a single party, i.e. Shores, and both were part of a single action. Shores consented to entry of judgment "in this action" without making any provision for appeal of any of the claims at issue. The defendants tendered an offer of judgment which offered "to allow judgment to be taken

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[5] In *United States Parole Commission* v. *Geraghty,* 445 U.S. 388, 402, 100 S.Ct. 1202, 1211, 63 L.Ed.2d 479 (1980), the Court stated that "[a] plaintiff who brings a class action presents two separate issues for judicial resolution. One is a claim on the merits; the other is the claim that he is entitled to represent the class."

against them ... in this action...." The offer made no reference to Shores' individual claims. Shores' acceptance stated without any qualification that he "hereby serves written notice that the 'Offer of Judgment', heretofore made by certain defendants is hereby accepted by the plaintiff." The acceptance similarly made no distinction between individual and class claims. The court order of judgment based on the parties' agreement entered "final judgment....in favor of the plaintiff" and provided that "this action be and it hereby is dismissed with prejudice as to [the other] defendants." The record indicates that Shores consented to entry of judgment encompassing the entire action.

The Ninth Circuit has addressed this precise issue. In *Seidman v. City of Beverly Hills,* 785 F.2d 1447 (9th Cir.1986), the district court denied Seidman's motion for class certification. Then Seidman settled his individual claim and stipulated to a dismissal with prejudice. The Ninth Circuit held that Seidman had agreed, not merely to dismiss his individual claim, but "to dismiss with prejudice the *action*" itself. 785 F.2d at 1448 (emphasis in original).

Applying the consent-to-judgment doctrine, the court dismissed the appeal. *See also Coughlin v. Regan,* 768 F.2d 468, 470 (lst Cir. 1985) (Where plaintiff consented to a judgment denying relief to a first subclass and granting relief to a second subclass, the court held that plaintiff's appeal was barred, explaining: "While it is possible for a party to consent to a judgment and still preserve his right to appeal, he must reserve that right unequivocally, as it will not be presumed.").

[4] Shores' contention that his consent to judgment should be presumed to have encompassed only his individual claims conflicts with the well-established principle that all interlocutory orders are merged into the final judgment. 9 J. Moore, B. Ward & J. Lucas, *Moore's Federal Practice,* ¶ 110.07, at 109 (1987); *Cohen v. Beneficial Industrial Loan Corp.,* 337 U.S. 541, 69 S.Ct. 1221, 93 L.Ed. 1528 (1949). Interlocutory orders denying class certification become part of the final judgment for purposes of appeal. *Coopers & Lybrand v. Livesay,* 437 U.S. 463, 98 S.Ct. 2454, 57 L.Ed.2d 351 (1978). Accordingly, in the absence of qualification,

consent to judgment constitutes consent to the interlocutory order denying class certification.

Love v. Turlington, 733 F.2d 1562 (11th Cir.1984), is not to the contrary. There the named plaintiff settled her individual claim, but reserved the right to appeal the district court's denial of class certification.[6] Because of this reservation there was no consent-to-judgment waiver in *Love*. It is clear from the opinion in *Love* that no such argument was made and the court did not address that issue. Rather, the *Love* court addressed a different issue, i.e., whether a named plaintiff who has settled her individual claim nevertheless retains a sufficient "personal stake" in the separate claim to represent the class. In other words the question addressed by *Love* was one of mootness. *Love* held that such a plaintiff does retain a sufficient "personal stake," and thus that the case was not moot and the court did

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[6] The court stated: "A settlement reached subsequent to the district court's denial of certification resolved plaintiff's individual claim.... It appeared that as a condition of the settlement of Love's individual claim, the defendants agreed not to contest the appealability of the certification order." 733 F.2d at 1564.

have subject matter jurisdiction of the named plaintiff's appeal. That holding is relevant in the instant case, and is controlling on that jurisdictional issue— i.e., absent his consent to judgment below, Shores would have had a sufficient stake to appeal the class certification issue notwithstanding the settlement of his individual claim. However, *Love is* not relevant to, and it did not address, the crucial issue on this appeal, i.e., whether Shores consented to judgment in the court below and thus is barred by the consent-to-judgment waiver doctrine.[7]

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[7] In *Love*, not only had the named plaintiff reserved the right to appeal the class certification issue, but in addition The defendant had agreed not to contest appealability. Thc court held that the latter—i.e., the defendant's waiver—was irrelevant to the jurisdictional issue, following the well-established principle that a party's consent cannot vest a court with subject matter jurisdiction that it does not have. Noting that the waiver of jurisdiction by the defendant in *Love* was irrelevant to the jurisdictional issue, Shores argues by analogy that it should be irrelevant in this case whether or not Shores consented to judgment, thus waiving his right to appeal. Shores' argument is intuitively suspect, because it would effectively eliminate the long-established consent-to-judgment waiver doctrine; that doctrine, and each case applying it, rests upon thc consent (i.e., waiver) of the party. The flaw in Shores' argument lies in The distinction between the two issues. In *Love*, the court was addressing its subject matter jurisdiction, i.e., whether the named plaintiff retained a sufficient personal stake in

III. CONCLUSION

For the foregoing reasons, we conclude that Shores consented to judgment in this entire action, and accordingly, the appeal is

DISMISSED.

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the case. In the instant appeal, thc issue is whether Shores will be permitted to challenge on appeal a judgment to which he consented in the district court This consent-to-judgment doctrine does not implicate the subject matter jurisdiction of the court, although the doctrine is sometimes cast in jurisdictional language, with references to the "standing" of the party to contest the issue on appeal. *See Dorse v. Armstrong World Industries, Inc.*, 798 F.2d at 1374 n. 3 ("Although this issue may be thought to be an issue of standing, it has been suggested that the applicable principle is instead waiver of error"); *Hunt v. Bankers Trust Co.*, 799 F.2d 1060, 1066 (5th Cir.1986) ("The banks contend . . . that a party will not be heard to appeal the propriety of an order to which it agreed. That is correct, but this objection relates to whether the appellate court will grant relief, and is not a basis to refuse jurisdiction"); 15 C. Wright, A. Miller and E. Cooper, *Federal Practice and Procedure* § 3902 at 408 (1976) ("Parties who have consented to entry of a judgment are at times said to lack standing to appeal, unless they can show facts that would justify nullifying the consent.... The true principle, however, appears to be properly explained in one of the early Supreme Court decisions as resting on waiver of error, leading to affirmance rather than dismissal: 'If, when thc case gets here, it appears that the decree appealed from was assented to by the appellant, we cannot consider any errors that may be assigned which were in law waived by the consent, but we must still receive and decide thc case. If all the errors complained of come within the waiver, the decree below will be affirmed, but only after hearing.'") (quoting *Pacific Railroad v. Ketchum*, 101 U.S. 289, 295, 251,.Ed. 932 (1880)) (footnotes omitted).

JOHNSON, Circuit Judge, specially concurring, in which KRAVITCH, HATCHETT and CLARK, Circuit Judges, join:

Under *United States Parole Comm. v. Geraghty*, 445 U.S. 388, 402, 100 S.Ct. 1202, 1211, 63 L.Ed.2d 479 (1980), the plaintiff who "brings a class action presents two separate issues for judicial resolution. One is the claim on the merits; the other is the claim that he is entitled to represent a class." The question presented in this case is whether Shores consented to judgment on both his claims. Specifically, this Court concludes Shores must have expressly reserved his right to appeal the district court's denial of class certification in consenting to entry of judgment in his original action in order to press this appeal. I concur in the majority's judgment for the following reasons.

This Court writes on a clean slate. No Eleventh Circuit or Supreme Court case is dispositive. We held in *Dorse v. Armstrong World Industries, Inc.*, 798 F.2d 1372 (11th Cir.1986), that parties who have consented to judgment may not appeal issues settled by that judgment unless they have expressly reserved the right to do so. In this case,

however, appellant argues that he did not consent to judgment on his class action claim. *See id.* at 1376 (citing 9 Moore, Federal Practice paragraph 203.06 at 3-27) ("[An appellant] may, however, urge on appeal that his consent was not actually given."). In *Love v. Turlington,* 733 F.2d 1562 (llth Cir.1984), we held that the settlement of a plaintiff's individual claim does not moot the individual's right to represent the class. However, the appellant in *Love* expressly reserved the right to appeal. Shores failed to do so.

The dispute in this case centers around interpreting the phrase "to allow judgment to be taken ... in this action." This Court can resolve the ambiguity by adopting one of two clear rules. First, a plaintiff bringing individual and class claims could be required to reserve expressly his or her right to appeal the denial of class certification. This is the approach chosen by the majority. Alternatively, a plaintiff could presumptively retain his right to appeal in the absence of an express waiver.

I write separately to note that the majority's choice

of rules should affect *only* Shores' right to appeal, because I think the reasoning of *United Airlines, Inc. v. McDonald,* 432 U.S. 385, 97 S.Ct. 2464, 53 L.Ed.2d 423 (1977), logically extends to protect the rights of the putative class members whom Shores purported to represent. I do not interpret the majority opinion as preventing interested members of the putative class from intervening under Rule 24[1] and appealing the district court's denial of class certification. At this point, it appears only Shores has lost his right to appeal the denial of class certification.

In *McDonald,* the Court held that a putative class member could intervene to appeal the denial of class certification within 30 days of entry of final judgment. In *McDonald,* a stewardess brought individual and class claims against United Airlines. Although class certification was denied, she prevailed on her individual claims and final

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[1] Fed.R.Civ.P. 24 reads:

(b) Permissive Intervention. Upon timely application anyone may be permitted to intervene in an action: (1) when a statute of the United States confers a conditional right to intervene; or (2) when an applicant's claim or defense and the main action have a question of law or fact in common.

judgment was entered. A member of the spurious uncertified class, another stewardess, moved to intervene 18 days after the entry of final judgment in order to appeal the denial of class certification. The Court held that her motion to intervene and appeal was timely and proper. It noted that the intervening stewardess made her motions "after learning that ... the [named] plaintiffs did not now intend to file an appeal challenging the District Court's denial of class certification." *Id.* at 390, 97 S.Ct. at 2467. The Court stressed "as soon as it became clear to the respondent that the interests of the unnamed class members would no longer be protected by the named class representatives, she promptly moved to intervene to protect those interests." *Id* at 394, 97 S.Ct. at 2470.

Until today, the putative class members in this case could reasonably have presumed that their interests were adequately and properly represented by Shores (and this Court so held in its vacated panel opinion). Today, members of the putative class will learn that their representative cannot appeal the denial of class certification. The reason

ing of *McDonald* suggests that they have the opportunity to intervene and appeal that order.[2] I concur in the majority's judgment with confidence that the logic of *McDonald* authorizes affected members of the putative class to make the proper motions below to intervene and appeal. [3] This decision should merely start the clock ticking on the timeli-

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[2] Intervention at the time of the denial of class certification would likely have been unavailing because appeals from such orders are interlocutory. The *McDonald* opinion aptly explains the impropriety of imposing a requirement of intervention at that point. See 432 U.S. at 394 n. 15, 97 S.Ct. at 2470 n. 15.

[3] Since the majority affirms the entry of final judgment, any members of the putative class who wish to intervene and file a notice of appeal of the denial of class certification will first have to move the district court to open the judgment under Fed.R.Civ.P. Rule 60(b). Rule 60(b) reads:

(b) Mistakes; Inadvertence; Excusable Neglect; Newly Discovered Evidence; Fraud,etc. On motion and upon such terms as are just, the court may relieve a party or a party's legal representative from a final judgment, order, or proceeding for the following reasons: (I) mistake, inadvertence, surprise, or excusable neglect ... (6) any other reason justifying relief from the operation of the judgment.

This case seems a likely candidate for Rule 60 relief. *See Laguana Royalty Co v. Marsh*, 350 F.2d 817, 823 (5th Cir. 1965) ("Rule 60(b) is to be construed liberally to do substantial justice.....The rule is broadly phrased and many of the itemized grounds are overlapping, freeing courts to do justice in hard cases").

ness of their intervention. [4]

The policy behind permitting intervention in *McDonald* and this case is supported by concerns of fairness and judicial economy. Members of the putative class may have foregone bringing their own suits in reliance on Shores' class claims. If the relevant statute of limitations has run, they may be left without recourse. *See Crown, Cork & Seal Co., Inc. v. Parker,* 462 U.S. 345, 354, 103 S.Ct. 2392, 2398, 76 L.Ed.2d 628 (1983) (class action tolls statute of limitation on individual claims only until the day class certification is denied). Just as importantly, the class certification question stands on the brink of final appellate resolution after years of litigation. It would be a tremendous waste of judicial resources to send plaintiffs who are not time-barred back to square one. The opportunity of the members of the putative

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[4] The timeliness of a motion to intervene is evaluated according to several equitable factors. *See Walker v. Jim Dandy Co.*, 747 F.2d 1360, 1365-66 (11th Cir.1984) (listing factors district court must consider). *McDonald* indicates that a motion to reopen judgment, intervene and appeal might have to be made within 30 days of the issuance of the mandate in this case. 432 U.S. at 390, 97 S.Ct. at 2467; *see also* Fed.R. App.P. 4(a).

class to intervene under Rule 24 would protect the interests of the class members and save courts from duplicative litigation. *See Deposit Guaranty Nat. Bank v. Roper*, 445 U.S. 326, 339, 100 S.Ct. 1166, 1174, 63 L.Ed.2d 427 (1980) (preventing appeal of class action "would invite waste of judicial resources by stimulating successive suits brought by others claiming aggrievement"). Shores' negligence in failing to expressly reserve his right to appeal should not prejudice the rights of those he sought to represent, especially when it appears that the district court erred in not certifying the class. *See Shores v. Sklar, et al.*, 844 F.2d 1485, 1492-95) (llth Cir.), *withdrawn* 855 F.2d 722 (1988) (class of investors should have been certified).

I concur in the judgment with the understanding that Shores consented to judgment only on *his claim* to represent the class. Until this Court's decision today, it was unclear whether Shores had waived his right to appeal the denial of class certification. Therefore, the Court's reasoning in *McDonald* suggests strongly that interested putative class members are not yet barred from making the proper

motions below to intervene and bring a proper appeal of the district court's denial of class certification.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT FOR THE
NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

CA75 -H-618-S

Clarence E. Bishop, Jr., Etc.,
Et Al.,
Plaintiffs,

vs .

Jerald H. Sklar, Et Al.,
Defendants.

MEMORANDUM OF DECISION

This action is before the court on the several pending motions of the defendants which motions collectively raise numerous grounds common to some, if not all, of the defendants; consequently the court will consider each motion as having raised each ground and each defendant as having joined in each motion. Furthermore, the motions themselves, the extensive and excellent briefs of counsel, and the oral argument heard herein have raised certain material issues which have a direct bearing on the ultimate disposition of the motions. Thus, the court will be required to consider matters outside the pleadings to resolve the mo-

tions and attendant issues. Accordingly, pursuant to Rule 12(b) of the Federal Rules of Civil Procedure, the motions to dismiss shall be treated as motions for summary judgment and disposed of as provided in Rule 56.

The initial complaint in this action was filed on May 16, 1975. During the next several months numerous motions, affidavits and discovery documents were filed culminating in an order entered on September 8, 1975, allowing the plaintiff to file an amended complaint. The plaintiff filed the "First Amended Complaint" on September 8, 1975. That filing set off a second round of motions, affidavits and discovery papers. On December 29, 1975, an order was entered dismissing all claims under the Securities Act of 1933 (15 U.S.C. §77a et seq.) and, treating the numerous motions to dismiss as motions for more definite statement, directing that the plaintiff file a second amended complaint within 120 days. This time period was later extended to June 1, 1976, at plaintiff's request. The "Second Amended Complaint" was filed on June 9, 1976.

Not surprisingly, the filing of the Second Amended Complaint initiated a third round of motions and affidavits.

Desiring either to resolve the issues presented or at the very least to move this action past the "motion to dismiss stage" where it had been stalled for approximately a year and a half after the initial complaint was filed, the court set the action down for special hearing on September 24, 1976. Subsequent to the September hearing, and the extensive oral argument presented at that time, the court set out an extended briefing schedule. At the requests of the parties, the briefing schedule was further extended, and while the briefing period is now concluded, the court is still receiving supplemental briefs. In any event, the court now has before it the pleadings, the motions with supporting documentation, the submitted briefs and supplements thereto, and the benefit of exhaustive oral argument of counsel and considers the issues to be ripe for a decision.

The Second Amended Complaint filed by the plaintiff, Clarence E. Bishop, Jr., both individually and on behalf of a described class of persons charges the defendants with violations of the Securities Exchange Act of 1934 (15 U .S.C. §§78a et seq.) and further invokes the pendent jurisdiction of this court to add a state cause of action for fraud.

Plaintiff Bishop's Individual Action

The plaintiff maintains that all his claims in the complaint are predicated on actions by the various defendants, either separately or in conjunction with one another, prior to, concurrent with, and/or subsequent to the issuance and/or sale of $1,500,000 principal amount of The Industrial Development Board of the Town of Frisco City, Alabama ("Board") First Mortgage Revenue Bonds, Series A, dated November 1, 1972 ("Bonds"). The Bonds were authorized and issued as coupon bonds in the denomination of $1,000 each, numbered serially from 1 to 1,500, and were to mature serially over a period of 20 years. Interest on the Bonds was to be paid semi-annually at varying coupon rates. The Bonds were issued and sold in three equal increments of $500,000 each to defendant Jackson Municipals, Inc. which served as underwriter for the Bonds. The sale of the first increment of the Bonds occurred on November 28, 1972 (or December 14, 1972); the second increment was sold on January 3, 1973; and the third and final increment of Bonds was sold on January 30, 1973.

The Bonds were issued by the Board to finance the construction and equipping of a manufacturing plant ("Plant") to be occupied by Alabama Supply and Equipment Company ("ASECO") under a long term lease ("Lease") from the Board. The rent ASECO was to pay was an amount calculated to amortize and retire the principal and interest on the Bonds. The Bonds were to be payable solely from the proceeds derived from the Lease and were secured by a Mortgage, Indenture of Trust and Security Agreement dated as of November 1, 1972 ("Indenture") from the Board to Phenix National Bank, Phenix City, Alabama ("Trustee Bank"), which is now the First Alabama Bank of Phenix City. The statutory authorization for the issuance and sale of the Bonds, the construction and leasing of the Plant, the execution of the Indenture and the general proceedings associated therewith is one of two general methods of municipal industrial development financing and is found in Sections 815, et seq. of Title 37 of the Code of Alabama, which statutory authority is commonly referred to as the Cater Act.

On January 19, 1973, plaintiff Bishop purchased

from Professional Securities, Inc. (which is not a defendant herein) Bonds numbered 593, 594 and 595 and on February 12, 1973, he purchased from the same source a fourth Bond serially numbered 619. Plaintiff paid par ($1,000) for each of the four Bonds, plus interest accrued thereon from the date of each Bond, November 1, 1972, to the date of purchase. Each of these four Bonds was a part of the second increment of Bonds sold January 3, 1973. He still owns each of the four Bonds.

As stated earlier, the motions before the court are addressed to the third effort of plaintiff to state a claim upon which relief can be granted. This effort, the "Second Amended Complaint, "carefully divides the defendants into various groups and endeavors to state claims against all defendants in three counts.[1] *Count I* attempts to state a cause of action for violation of Section 10(b) of the 1934 Act and of Rule 10b-5 promulgated in connection therewith, and this court clearly has jurisdiction over this cause of action and the

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[1] It may be that the "Candler Defendants" are not intended to be defendants to Count I. Clearly all other defendants are included in Count I and all defendants are joined in Count II and Count III.

parties thereto. In essence it charges that the Bonds were sold by means of an Offering Circular which contained untrue statements of material facts and which omitted material facts which are necessary and that the defendants were responsible for the false statements and omissions in the Offering Circular.[2] *Count III* is a wholly state law based caused of action for fraud. There is no independent basis for this court to entertain jurisdiction over the parties to and cause of action stated in Count III. Thus jurisdiction, if it exists, is pendent to the Rule 10b-5 action stated in Count I.[3] *Count II* really adds nothing to the complaint. It simply alleges a "conspiracy" by the defendants to violate Rule 10b-5 or to commit common law fraud or to do both.

While Count I alleges that the Bonds were sold by

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[2] The court here assumes, without deciding, that the requisite mental state or scienter has been alleged, although with regard to most of the defendants this may well be an unfair assumption. See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976).

[3] It will not be necessary for the court to resolve the serious jurisdictional question applicable to some defendants, primarily Trustee Bank and the "Candler Defendants." But clearly if they are not proper defendants under Count I, this court would not have jurisdiction of the Count III claim against them. *Aldinger v. Howard*, 427 U.S. I (1976).

means of an Offering Circular which contained untrue statements of material facts or which ommitted to state material facts which were necessary, it totally fails to allege that plaintiff Bishop relied upon the Offering Circular when he purchased his four $1,000 Bonds. Were the court dealing with a mere oversight in pleading, the matter would be simple—plaintiff would be permitted to amend and allege reliance. But the failure to allege reliance has been repeatedly driven home to plaintiff for an entire year and he has failed to endeavor to amend. The reason for this failure, as will be discussed hereafter, is that Mr. Bishop did not rely on the Offering Statement, except perhaps in a most indirect manner. Thus the instant action squarely raises the issue of the extent to which reliance is a necessary element in a private securities fraud action. Plaintiff, relying primarily upon *Affiliated Ute Citizens v. United States,* 406 U.S. 128 (1972), asserts that to the extent that reliance is an element, that element is present. Defendants, quite naturally, take a contrary view.

Much of the controversy surrounding the question of reliance is predicated upon the difficulty of proving reliance

in omission as opposed to misrepresentation cases and open market versus face-to-face transactions. See, 2 Bromberg, *Securities Law*, §8.6(1)-(2), pp. 209-212; Jennings and Marsh, *Securities Regulation*, 4th ed., pp. 1060-1068 (1977). No such difficulty is presented in the instant action.

All of the plaintiff's allegations of fraudulent misrepresentations or omissions are focused on the Offering Circular prepared in connection with the initial sale of the Bonds and, as noted earlier, Mr. Bishop purchased four Bonds at par in a face-to-face transaction from a broker who is not a defendant. The Second Amended Complaint, however, in no way can be construed as alleging that Mr. Bishop relied upon the Offering Circular (and hence was defrauded by any false statements or omissions therein), and as a matter of fact, as will be discussed hereafter, Mr. Bishop never saw the offering Circular, AESCO, the Plant, the Board, the Lease or the Indenture, and did not rely on the Offering Circular. Thus, for the purpose of the pending motions the court can assume that every statement in the Offering Statement was material and false and that there was omitted from the Offering Statement numerous statements

of material facts necessary to be made in order to make the statements therein contained not misleading. For the real issue is whether a private securities fraud action will lie under Rule 10b-5 or whether a common fraud action will lie under state law in the face of an affirmative denial by the plaintiff of any reliance on the alleged fraudulent statements or omissions. The answer is clear. Neither such action will lie and plaintiff may not recover.

On August 19, 1975, defendants Thomas E. Martin, Robin B. Page and Joseph F. Savage, propounded a set of interrogatories to plaintiff Bishop. On March 26, 1976, Mr. Bishop filed his sworn answers to those interrogatories. The following questions were asked and answers given:

[Question]

> I. MPS-17. Did plaintiff have any communications (oral or written) with anyone about TCC, the Offering Circular, ASECO and/or the Bonds?

[Answer]

> I. MPS-17. I did not have any communications with anyone about TCC. I never saw the Offering Circular or Offering Statement that has been identified to me by my attorneys. I had no communications with anyone about "ASECo". I did talk to Tom Monks at the time I purchased the bonds.

[Question]

> I. MPS-18. If the answer to Interroga-

tory 1. MPS-17 is in the affirmative:

(a) Identify each person with whom each such oral or written communication was held;

(b) Identify each person who was present during each such oral communication;

(c) State the date of each oral communication and where it took place;

(d) Set forth substance of what each person stated at each such communication and identify the speaker;

(e) Identify the person who initiated the topic referred to above in any oral communication;

(f) Identify each document which refers to, related to, records or evidences each such oral communication;

(g) Identify each written communication giving its date, author and all recipients thereof.

[Answer]

I. MPS-18 (a) Tom Monks who was president of Professional Securities, Inc ., 1620 - 10th Avenue South, Birmingham, Alabama 35205.

(b) Mr. Monks' secretary, whom I do not know.

(c) Immediately prior to the purchase of the first bonds and later when I made the second purchase. These communications were in Mr. Monks' office and by telephone.

(d) Mr. Monks advised me that these were tax free bonds and a good investment. He also told me about other people in the community who had purchased them.

(e) Mr. Monks.

(f) The confirmation of sales on the two purchases.

* * *

[Question]

I. MPS-28. Identify each document which plaintiff saw prior to making the acquisition and/or of which plaintiff was aware (even if plaintiff did not see it) which related to the Bonds, TCC and/or the acquisition and for each such document:

* * *

[Answer]

I. MPS-28. 1 did not see any or have knowledge of any, nor was I aware of any such document.

[Question]

I. MPS-34. Did plaintiff discuss plaintiffs' acquisition of the Bonds or the Offering Circular with anyone?

[Answer]

I. MPS-34 and 35. 1 may have casually mentioned the purchase of the bonds in conversation with friends or acquaintances. There was never any discussion other than a passing reference to the purchase of the bonds. There was no discussion of the bonds in the sense called for by the question. I am unable to recall, definitely, any specific person or occasions when I even occasionally mentioned the

bonds .

Thus the plaintiff has affirmatively denied seeing or relying on the Offering Circular that is the crux of the alleged fraudulent misrepresentations and omissions. In the light of a specific disavowal of reliance, plaintiff cannot prevail. And *Simon v. Merrill Lynch, Pierce, Fenner and Smith, Inc.*, 482 F.2d 880 (5th Cir. 1973), specifically rejects plaintiff's argument that *Affiliated Ute, supra,* eliminated the element of reliance in securities fraud action. The court held "that some element of general reliance, even in nondisclosure cases, is essential to a Rule 10b—5 action .... The circuit's requirement of reasonable reliance, therefore, was not met . " 482 F.2d at 884-85. The essentiality of the reliance element was reaffirmed in *Vohs v. Dickson,* 495 F.2d 607, 622 (5th Cir. 1974), where the court again concluded that even in instances of alleged fraudulent omissions a general reliance must be shown. In the instant action plaintiff has specifically denied *any* reliance— general or specific. He has denied seeing the Offering Circular, he has denied talking with anyone about ASECO; or, indeed, inquiring about the Bonds other than being told that they were tax free and a good investment.

The securities laws were not intended to be an absolute insurance policy to investors. The purpose of the laws is to prevent fraud of the reasonable and prudent investor, they were not intended to protect investors from their own shortcomings or failures to inquire and investigate. Private securities violations are predicated on fraud and the necessary elements must be plead and proven or no recovery will lie. *Ernst & Ernst v. Hochfelder,* 425 U.S. 185 (1976). Also see FRCP Rule 9(b).

The plaintiff herein in a sworn statement has denied that he relied on the Offering Circular or on any significant oral representation. Moreover, he cannot successfully argue any "open-market" relaxation of the reliance requirement[4] because he purchased his Bonds, at par, over-the-counter, as a part of the distribution of an initial issue and not in any secondary market or on a national securities exchange. Some form of reliance is an essential element of a Rule 10b-5 action. *Simon v. Merrill Lynch, Pierce, Fenner and Smith, Inc., supra; Vohs v. Dickson supra.* No form of reliance is

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[4] See *Blackie v. Barrach,* 524 F.2d 891 (9th Cir. 1975). But see *Little v. First California Company,* 532 F.2d 1302 (9th Cir. 1976).

present here. There is no genuine issue as to any material fact concerning the absence of reliance and the defendants are entitled to a judgment as a matter of law against plaintiff Bishop under Count I. Because reliance is also a required element of both common law fraud, see, Prosser, *Law of Torts* 4th ed., §1 8 1971), and statutory fraud or deceit in Alabama, see e.g., *Hudson v. Moore,* 239 Ala. 130, 194 So. 147 (1949); *Old Southern Life Ins. Co. v. McConnell,* 52 Ala. App. 589, 296 So.2d 183 (1974), defendants are also entitled to a judgment as a matter of law against plaintiff Bishop under Count III. Necessarily a judgment against plaintiff Bishop on Counts I and III will mandate a similar judgment under Count II.

Class Action Matters

Plaintiff Bishop, as the only named representative of the class, also pursues this action on behalf of a purported class consisting of "all . . . persons who, to their injury and damage, purchased First Mortgage 8% Revenue Bonds, Series A, . . . issued by The Industrial Development Board of the Town of Frisco City, Alabama." The fact that Mr.

Bishop cannot prevail on his individual action does not prevent him from pursuing the class aspect of this action, provided that the action may otherwise proceed as a class action. And while even the claims of the class, as a pure pleading matter, should be dismissed as totally lacking in the necessary allegations of reliance, the court is of the opinion that the class questions should be more directly addressed.

There is no question that securities fraud actions are often well suited for treatment as class actions. "On the other hand, although having some common core, a fraud case may be unsuited for treatment as a class action if there was material variation in the representations made or in the kinds or degrees of reliance by the persons to whom they were addressed." Ad*visory Committee Report on the Proposed Amendments to the Rules of Civil Procedure,* 39 F.R.D. 69, 103 (1966). And before permitting a suit filed under Rule 23 of the Federal Rules of Civil Procedure to be maintained as a class action, the court must be satisfied that the prerequisites of Rule 23 have been met. Plaintiff has not so satisfied the court.

Absence of typicality and adequate representation are apparent, and there is nothing before the court upon which it can conclude that common questions of fact predominate. Plaintiff twice has been afforded the opportunity completely to amend the complaint; has had over two years to engage in discovery; and has been reminded time after time by defendants during the past year of the total absence in the complaint of any allegation of reliance, not only as to Mr. Bishop but also as to the class he seeks to represent. He has not endeavored to determine the extent to which, if at all, any member of the putative class may have relied on the Offering Statement. Indeed, he has not communicated with any class member. See plaintiff's March 26, 1976 answers to interrogatory 1. MPS-22 propounded August 19, 1975 by defendants Martin, Page and Savage. The evident lack of interest of plaintiff in determining if any other purchaser saw the Offering Circular or relied in any manner thereon is best understood by Mr. Bishop's personal interest in pursuing his own claim, where reliance was non-existent, in a manner inconsistent with the possible claims of putative class members who may have relied upon the Offering

Circular, albeit in significantly varying degrees and circumstances. Accordingly, pursuant to Rule 23(c) a separate order will be entered prior to the judgment against plaintiff Bishop that this action shall not be maintained as a class action. Because this Rule 23(c) determination is being made over two years after the action was filed (it took plaintiff over a year to finally draft a complaint which he wanted to rest on, it took the parties six months to brief the issues and it took the court over six months to resolve the issues), statutes of limitations may adversely affect individual rights of the putative class. Accordingly, the order to be entered will expressly authorize any putative class member, within six months after the entry of such order, to petition the court to intervene in this action to pursue his *individual* claim. Jurisdiction will be retained for the limited purpose of considering such a petition and, where the petitioner satisfies the court that he failed to pursue his individual claim in reliance upon this action being pursued for his benefit, the intervention will be allowed as if it had preceded the Rule 23(c) determination. This retention of jurisdiction for the limited purpose of possibly adding additional parties plain-

tiff shall not affect the finality or appealability of the judgment to be rendered against plaintiff Bishop since under Rule 54(b) the court expressly determines that there is no just reason for delay and expressly directs the entry of such final judgment.

An appropriate order and an appropriate judgment will be entered.

DONE this 2nd day of August, 1977.

/s/ James H. Hancock

UNITED STATES DISTRICT JUDGE

FINAL JUDGMENT

In accordance with the Memorandum of Decision entered this day it is hereby

ORDERED, ADJUDGED and DECREED that plaintiff Clarence E. Bishop, Jr. have and recover nothing of defendants.

Costs are taxed against the plaintiff.

DONE this 2nd day of August, 1977.

/s/ James H. Hancock
United States District Judge

APPENDIX C

James L. SHORES, Jr., as Executor of the Estate of Clarence E. Bishop, Jr., etc., et al., Plaintiffs-Appellants

Jerald H. SKLAR et al., Defendants-Appellees

No. 77-2896.

United States Court of Appeals
Fifth Circuit.

Jan. 21, 1980.

Appeal from the United States District Court for the Northern District of Alabama.

Before SIMPSON, CHARLES CLARK, and FRANK M. JOHNSON, Jr., Circuit Judges.

CHARLES CLARK, Circuit Judge:

Clarence E. Bishop, Jr., brought this action in the Northern District of Alabama on behalf of himself and the class of all purchasers of First Mortgage Revenue Bonds issued by the Industrial Development Board of the Town of Frisco City, Alabama, seeking to recover upon default on the bonds. After twice allowing Bishop to amend his complaint, the district court entered summary judgment for the defendants, holding that Bishop's failure to allege that he relied

upon any of the defendants' misrepresentations or omissions was fatal to his claim. Bishop died during the pendency of the case and his executor appeals. We hold that the plaintiff's allegations state a claim of fraud so pervasive that the absence of reliance was not dispositive of the case. Because genuine issues of material fact remain to be tried, we reverse the judgment entered and remand the case for further proceedings.

The Cater Act, Ala.Code tit. 37, § 815 et seq., authorizes the incorporation of an Industrial Development Board [Board] in a municipality in order to induce industry to locate in Alabama. *Id.* § 816. Such a board has the authority to issue tax-exempt bonds. *Id.* §§ 822, 825. With the proceeds of such an issue, the Board can build an industrial facility, which it may then lease to a manufacturing, industrial, or commercial enterprise. *Id.* § 822. The amount of the rental payments is calculated to amortize the interest and principal of the bonds and is ostensibly lower than that which could be obtained without tax-free financing.

The bonds are revenue bonds, not general obligation bonds of the municipality. They must be secured by a pledge

of the revenues and receipts from the lease and may be further secured by a mortgage or deed of trust covering the project from which revenues are to be derived. *Id.* § 824. The municipality is in no event liable for the payment of any of the Board's obligations, *id.* § 826; interest and principal are payable solely from the lessee's rent payments. *Id.* § 823.

The bond issue in question began when J. C. Harrelson, president and sole shareholder of Alabama Supply and Equipment Company [ASECo], and Clarence Hamilton, president of Investors Associates of America, Inc., a Tennessee underwriter, decided to seek industrial development financing to locate a facility in Frisco City, Alabama. Hamilton retained Jerald H. Sklar, of the Memphis, Tennessee, law firm of Waring, Cox, James, Sklar & Allen, as bond counsel. Sklar instructed Investors Associates to conduct an investigation of ASECo and retained John Andrews, of Capell, Howard, Knabe & Cobbs, P.A., a Montgomery, Alabama, law firm, as bond co-counsel. Andrews saw to the incorporation of the Industrial Development Board of Frisco City and issued an opinion on the legality of the authorization and issuance of the bonds. Sklar drafted the lease,

indenture of trust, mortgage, authorizing resolution, guarantee, and closing papers. Hc also drafted the offering Circular, based on information furnished to him by thc underwriter, the lessee company, and those associated with them. Part of the information Sklar incorporated into the Offering Circular was a financial statement prepared by George C. Rakerd, a certified public accountant.

Plaintiff alleges that thc Rakerd financial statement contained material misrepresentations and omissions. Hc asserts, for example, that certain investment real-estate, which was recorded as an asset having a value of $2,420,500, was property in which ASECo had no ownership interest at thc time the financial statement was certified. Plaintiff alleges that Rakerd's certification of thc financial statement as made in accordance with generally accepted auditing standards was either knowingly or recklessly false, for Rackerd made no independent inquiry. Plaintiff further alleges that these misrepresentations or omissions in the financial statement were included in the Offering Circular and further amplified therein. The financial statement also included as assets certain receivables owed by J. C. Harrel-

son to ASECo, which, plaintiff alleges, were of little value because Harrelson was in default on at least one of the notes at the time of certification.

Investors Associates determined that it did not possess sufficient capital to underwrite the proposed issue and assigned the right to underwrite the issue to Jackson Municipals, Inc., a Tennessee underwriting firm headed by Cecil Lamberson. The Phenix National Bank (now the First Alabama Bank of Phenix City, N.A.) had been chosen to act as trustee of the bond proceeds. The bank was also to ensure that the lessee complied with the terms and conditions of the lease, one of which was that ASECo at all times have working capital in the amount of $400,000.00 or more. Plaintiff alleges that the bank knew or should have known that ASECo was in breach of that provision of its agreement from the inception of the lease.

The Industrial Development Board of Frisco City adopted the resolution authorizing the bond issue. The Board entered into an agreement with Coliseum Properties, Inc., to construct part of the facilities contemplated by the bond issue. Plaintiff alleges that Coliseum Properties, Inc.,

did no more than serve as a vehicle by which substantial parts of the proceeds of the issue were diverted and used for the benefit of others. In particular, plaintiff alleges that the controlling persons of the parent corporation of Coliseum Properties [the Candler defendants] made improper payments to ASECo and to Harrelson in exchange for the construction contract; moreover, Coliseum Properties and some of its officers were under indictment in several pending suits. None of this information was disclosed to the Board when it entered into its agreement with Coliseum Properties.[1]

Jackson Municipals purchased the entire issue in three increments and resold them to other dealers. Plaintiff Bishop purchased his bonds from Professional Securities, Inc., a Birmingham municipal securities dealer, not here made a defendant. Bishop did so solely on the basis of the oral representations of his broker that the tax-free bonds would be a good investment. He never saw the Offering

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[1] Bishop named all of the parties mentioned above as defendants except J. C. Harrelson, who was murdered before the commencement of this action; John Andrews; and Coliseum Properties, Inc.

Circular. After the plant had been constructed, the lessee ceased operation at the plant and defaulted in payment of rent under the lease on April 15, 1974. Although Harrelson had unconditionally guaranteed the performance of the lease by ASECo, he did not have sufficient assets to back up his guarantee. The Trustee Bank declared default in the lease. The bonds became worthless. Bishop then brought this action.

The initial complaint in this action raised claims under the Securities Act of 1933, 15 U.S.C. § 77a et seq., and the Securities Exchange Act of 1934, 15 U.S.C. § 78a et seq., and pled a pendant Alabama state-law fraud claim. As a result of the numerous motions, affidavits, and discovery documents that were filed, the court permitted the plaintiff to amend his complaint twice but dismissed all claims under the 1933 Act. After the plaintiff filed his second amended complaint, the defendants moved to dismiss for failure to state a claim because Bishop did not allege that he relied upon the Offering Circular. Bishop filed all complaints both individually and on behalf of the class of all purchasers of the bonds.

The complaint purports to state claims against the defendants in three counts. Count I attempts to state a cause of action for violation of § 10(b) of the 1934 Act and of Rule 10b-5 promulgated thereunder. In essence it charges that the bonds were sold by means of an Offering Circular that contained untrue statements of material fact and which omitted material facts that were necessary to make other statements made not false or misleading and that these misstatements and omissions appeared in the Offering Circular only as a result of the culpable behavior of the defendants. Count II essentially alleges that the defendants engaged in a conspiracy, scheme, or agreement to do those things complained of in Count I. Count III alleges that the same conduct is actionable under Alabama common-law fraud.

In *Simon v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 482 F.2d 880 (5th Cir. 1973), we stated that "some element of general reliance by plaintiff, even in nondisclosure cases, is essential to a Rule 10b-5 action." *Id.* at 884. The district court relied on this language to deny recovery to the plaintiff. Taking into consideration answers to inter-

rogatories in which the plaintiff "affirmatively denied seeing or relying on the Offering Circular," the court concluded that no reliance was present and that there existed no genuine issue concerning the absence of reliance.

In *Rifkin v. Crow*, 574 F.2d 256 (5th Cir. 1978), decided after the district court's opinion, the same judge who wrote *Simon* explained that *Simon* was a fact case that hinged on the nature of the so-called "Ute presumption" established for nondisclosure cases. In *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 92 S.Ct. 1456, 31 L.Ed.2d 741 (1972), the Supreme Court held that the plaintiffs' inability to prove reliance did not bar recovery. *Simon* pointed out that *Ute* did not do away with reliance as an element of a 10b-5 case, noting that *Ute* did not involve "a general lack of reliance by the plaintiffs on the defendants' representations 482 F.2d at 884. *Rifkin* further clarified this circuit's construction of *Ute*. It held that *Ute* merely established a presumption that the plaintiff would have relied on material information which the defendant failed to disclose, a presumption. *Simon* held to be rebuttable.

[1] *Simon's* emphasis on reliance may have dis-

tracted the district court from the essential element of recovery, causation. Reliance is essential only if it plays a part in causation. *Rifkin* illustrates that causation is the basis of liability: "*Simon's* 'general reliance' language simply requires there to be a causal link between defendant's violation and plaintiff's harm in order for plaintiff to recover." 574 F.2d at 261 n. 1.

[2, 3] In a nondisclosure case, if the defendant can show that the plaintiff's decision would not have been affected by disclosure of the material information, then the defendant played no part in causing those losses and cannot be held liable for them. Were plaintiff's claim here a run-of-the-mill nondisclosure case, the district court's position might have been correct.[2] If plaintiff claimed no more than that the inclusion of material information in the Offering

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[2] The defendants moved to dismiss under Fed.R.Civ.P. 12(b)(6) for failure to state a claim. Because the district court considered matters outside the pleadings, the motions to dismiss were treated as motions for summary judgment but without the rule-required notice to the parties. Fed RCiv.P. 12(b) & 56. *See, e. g., Underwood v. Hunter*, 604 F.2d 367 (5th Cir. 1979). Bishop urges the absence of notice as reversible error. In view of our disposition of the merits of the appeal, we need not decide this procedural issue.

Circular would have kept him from purchasing the bond, then his admission that he placed no reliance whatsoever upon the Offering Circular would bar his recovery. In such a case, as in *Simon*, the nondisclosure would simply not have caused his loss.

But plaintiff alleges much more than a misrepresentation or nondisclosure that influenced price. He alleges that the bonds could never have been marketed if any of the defendants had disclosed the material information. In this sense, the plaintiff's theory is very similar to the fraud-on-the-market theory that has developed in cases involving price-rigging in connection with the sale of stock. See, e. g, *Zweig v. Hearst Corp.*, 594 F.2d 1261 (9th Cir. 1979); *Blackie v. Barrack*, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816, 97 S.Ct. 57, 50 L.Ed.2d 75 (376); *Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374, 381 (2d Cir. 1974), *cert. denied*, 421 U.S. 976, 95 S.Ct. 1976, 44 L.Ed.2d 467 (1975).

[4] The trial court, believing the fraud-on-the-market theory to be an "open-market" relaxation of the reliance requirement, held that Bishop could not recover because he purchased his bonds over the counter as part of the distribu-

tion of an initial issue and not in any secondary market or on a national securities exchange. The requirement of a secondary market is important to a price-rigging fraud-on-the-market case, for that theory relies on the market to employ all available information (including misrepresentations or as affected by material omissions) in setting the price of a stock.

[5] Such a market is irrelevant here, however, for Bishop does not allege that the price at which he purchased the bonds was distorted by misrepresentations or omissions. He argues instead that the very issuance of the bonds was dependent on those misrepresentations and omissions. A secondary market would play no part in the defendants' ability to float the issue, even though it might determine the price at which the bond was subsequently traded.

What is important here are the procedures, whether statutory or traditional by which a bond issue can successfully be floated. Just as the purchaser of a stock on the open market can expect the market to reflect all information about that stock, so, too, can the purchaser of a new bond issue expect these procedures—the underwriter's investi-

gation and report the accountant's certified financial statement, bond counsel's opinion letter, and the like—to have been faithfully performed. In a stock case, a fraud on thc market would affect the price; here, the fraud asserted would affect whether the issue could ever go forward at all.

In a fraudulent scheme of the magnitude of that alleged, plaintiff's lack of reliance on the Offering Circular is irrelevant. In a more ordinary fraud case lack of reliance would generally imply lack of causation. Here, however causation is clearly present irrespective of plaintiff's reliance on thc Offering Circular. The scheme to float the bond issue was thc cause in fact of plaintiff's losses, for if the defendants had not engaged in thc fraudulent behavior, the bond would never have been offered for sale, plaintiff could not have purchased it, and no loss would have resulted. Because plaintiff's allegations, if true, would support a finding that the defendants' misrepresentations and nondisclosure of material information acted to perpetrate a fraud by allowing to be offered for sale a bond issue that would otherwise not have succeeded, he is entitled to proceed beyond the pleading stage to attempt to prove his

allegations.

We do not undertake to chart the entire course for the remanded cause from that point except to say briefly that ultimate liability may turn on other matters, such as whether defendants acted with requisite scienter and, if less than totally debilitating fraud can be proved, whether some material falsity that may have affected some of the bond's terms but would not have prevented its issuance would still require proof of reliance. All we say for this appeal is that plaintiff is entitled to attempt to prove the case he has alleged.

Thc district court also dismissed the plaintiff's claim for relief under Alabama common-law fraud. The authorities cited by the district court in its opinion did not purport to deal with the kind of situation present here but were traditional misrepresentation cases. Accordingly, thc court should reconsider plaintiff's state-law claim, taking into account our discussion above and the facts adduced at trial. The court also ruled that this action could not be maintained as a class action because of lack of typicality, lack of adequate representation, and lack of a showing that common

questions of fact would predominate. All three of these determinations, however, were premised on the belief that reliance on the Offering Circular was crucial to plaintiff's claim on remand, the court must also reconsider the maintainability of this action as a class action.

REVERSED and REMANDED.

APPENDIX D

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

U.S. COURT OF APPEAL
FILED
May 2, 1980
Gilbert F. Ganucheau
Clerk

No. 77-2896

JAMES L. SHORES, JR.as
Executor of the Estate of
CLARENCE E. BISHOP, JR., ETC.,
ET AL.,

Plaintiffs-Appellants,

versus

JERALD H. SKLAR, ET AL.,

Defendants-Appellees.

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Appeal from the United States District Court for the
Northern District of Alabama

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ON PETITION FOR REHEARING AND PETITION FOR
REHEARING EN BANC
(Opinion Jan 21, 1980, 5 Cir., 1980, 610 F.2d 235).

(May 2, 1980)

Before COLEMAN, Chief Judge, BROWN, AINSWORTH,
CHARLES CLARK, RONEY, GEE, TJOFLAT,
HILL, FAY, RUBIN, KARVITCH, FRANK M.
JOHNSON, JR., GARZA, HENDERSON,
REAVLEY, POLITZ, HATCHETT, ANDERSON,

RANDALL, TATE, SAM D. JOHNSON and THOMAS A. CLARK, Circuit Judges. *

BY THE COURT:

A member of the Court in active service having requested a poll on the application for rehearing en banc and a majority of the judges in active service having voted in favor of granting a rehearing en banc,

IT IS ORDERED that the cause shall be reheard by the Court en banc with oral argument on a date hereafter to be fixed. The Clerk will specify briefing schedule for the filing of supplemental briefs.

*Judges Godbold and Vance have recused themselves and did not participate in this decision.

APPENDIX E

James L. Shores, Jr., as Executor of
The Estate of Clarence E. Bishop, Jr.,
etc., et al., Plaintiffs-Appellants,

v.

Jerald H. Sklar et al.,
Defendants-Appellees .

No. 77-2896.

United States Court of Appeals,
Fifth Circuit.

May 26, 1981.

Appeal from the United States District Court for the Northern District of Alabama.

Before BROWN, COLEMAN, AINSWORTH, CHARLES CLARK, RONEY, GEE, TJOFLAT, HILL, FAY, RUBIN, KRAVITCH, FRANK M . JOHNSON, Jr., GARZA, HENDERSON, REAVLEY, POLITZ, HATCHETT, ANDERSON, RANDALL, TATE, SAM D. JOHNSON, and THOMAS A. CLARK, Circuit Judges.*

CHARLES CLARK, Circuit Judge:

Clarence E. Bishop, Jr., was one of a number of purchasers of First Mortgage Revenue Bonds of the Indus-

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* Chief Judge Godbold and Judge Vance were disqualified in this case. Judge Williams does not wish to participate in the decision.

trial Development Board of Frisco City, Alabama ["Bonds"]. The lessee of the industrial business premises, the sole source of the income necessary to amortize the revenue Bonds, almost immediately defaulted in the payment of rent, causing the value of the Bonds to drop precipitously. [1] Bishop sued most of those involved with the issuance of the Bonds, alleging that he was the victim of a pervasive scheme to defraud members of the investing public in violation of the securities laws. In essence, the complaint alleged that the defendants had fabricated a materially misleading Offering Circular in order to induce the Industrial Development Board ["Board"] to issue, and the public to buy, fraudulently marketed bonds.[2]

After twice allowing Bishop to amend his complaint, the district court entered summary judgment for the defen-

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[1] After the sale of the lessee's plant, the identifiable Bond holders received $373.33 per $1000 bond.

[2] Throughout the opinion we refer to these Bonds as being "fraudulently marketed." This means the fraudulent scheme alleged by Bishop was so pervasive that without it the issuer would not have issued, the dealer could not have dealt in, and the buyer could not have bought these Bonds, because they would not have been offered on the market at any price.

dants. Based on Bishop's statement in his answers to interrogatories that he never saw nor was he aware of the Offering Circular when he decided to purchase the Bonds, the district court concluded that Bishop had in no way relied on the Circular's alleged misrepresentations or omissions and that his lack of reliance was fatal to his claim. We reheard this case en banc to determine whether a plaintiff must rely specifically on material misrepresentations or omissions in a single disclosure document when, in addition to charges based on its untrue statements or misleading omissions, other allegations would admit proof that the existence of the security in the marketplace resulted from the successful perpetration of a fraud on the investment community and that he purchased in reliance on the market. We hold the securities laws and regulations have a purpose broader than merely criticizing ever-lengthening, complex prospectuses. They cover deliberate, manipulative schemes to defraud which can annul not only the purpose of disclosure but also the market's honest function. Since plaintiff's pleadings would permit such proof, his suit should not have been dismissed at this initial stage. Accordingly,

we vacate the judgment of dismissal and remand the case for further proceedings.

I.

During the nearly two years from the time Bishop filed his complaint until the district court entered final judgment, this case did not proceed past the pleading and discovery stage. The court, on the defendants' motions to dismiss, considered matters outside the pleadings, treated the motion as one for summary judgment,[3] and entered judgment for the defendants, because the discovery materials considered showed there to be no genuine issue as to the fact of Bishop's lack of reliance on the Offering Circular. In considering the propriety of summary judgment, plaintiff's factual version must be taken as true. *Bishop v. Wood,* 426 U.S. 341, 347, 96 S.Ct. 2074, 2079, 48 L.Ed.2d 684, 691 (1976); *E. C. Ernst, Inc. v. General Motors* Corp., 537 F.2d 105, 108 (5th Cir. 1976).

The only fact material to the decision of the district

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[3] Fed.R.Civ.P. 12(b) and 56.

court in dismissing Bishop's complaint was that he did not rely on statements or omissions in the Offering Circular. While that admission correctly controlled the disposition of Bishop's claim that the Circular contained material misrepresentations and omissions (see Part III), we hold its consideration was improper in determining to dismiss his claim based on fraud in bringing the bonds into the marketplace (see Part IV). Therefore, in regard to the latter claim, the dismissal is truly on the pleadings alone. Under *Conley v. Gibson*, 355 U.S. 41, 45, 78 S.Ct. 99, 101, 2 L.Ed.2d 80 (1957), review of the dismissal of this part of the complaint requires us to determine whether Bishop could prove any set of facts in support of his claim which would entitle him to relief.

Reciting the facts most favorably to the plaintiff, as we do below, does not imply that he can prove his allegations.

II.

The bond issue in question had its genesis in 1972 when J. C. Harrelson, president and chief shareholder of

Alabama Supply and Equipment Company [ASECo], and Clarence Hamilton, president of Investors Associates of America, Inc., a Tennessee underwriter, decided to seek industrial development financing to construct and equip a facility for the construction of mobile homes in Frisco City, Alabama. Alabama law provides for such financing pursuant to the Wallace-Cater Act, codified in §§ 11-54-80 *et seq.*, Code of Alabama (1975), which authorizes the incorporation of an Industrial Development Board in a municipality in order to induce industry to locate in Alabama. *Id.* § 11-54-81. Such a board has the authority to issue taxexempt bonds. *Id.* §§ 11-54-87, 11-54-96. With the proceeds of such an issue, a board can build an industrial facility, which it may then lease to a manufacturing, industrial, or commerical enterprise. *Id.* § 11-54-87. The amount of rental payments is calculated to amortize the interest and principal of the bonds and is ostensibly lower than that which could be obtained without tax-free financing.

The Bonds are revenue bonds, not general obligation bonds of the municipality. They must be secured by a pledge of the revenues and receipts from the lease and may be

further secured by a mortgage or deed of trust covering the project from which revenues are to be derived. *Id.* §§ 11-54-90. The municipality is in no event liable for the payment of any of a board's obligations, *id.* § 11-54-92; the sole source for the satisfaction of interest obligations and retirement of principal is the lessee's rent payments. *Id.* § 11-54-89.

Neither Harrelson nor ASECo was a paragon of financial integrity or industrial ability. Harrelson had been only moderately successful in previous business ventures and had little experience in the development of plants for the construction of modular or mobile homes. ASECo's management was inept and unsophisticated, its projections for the sales of mobile homes were mere marketing assumptions, and its financial condition was weak. Indeed, Harrelson and Hamilton both knew that ASECo did not have the financial capability to engage in the manufacture of mobile homes and related products or to pay the rent necessary to amortize the principal and interest on the Bonds. Nevertheless, they determined to induce the Town of Frisco City to create an Industrial Development Board to finance ASECo's facility as a scheme to defraud the investing public.

Hamilton retained defendant Jerald H. Sklar, a Tennessee attorney, as bond counsel. Sklar instructed Investors Associates to conduct an investigation of ASECo and retained John Andrews of Capell, Howard, Knabe & Cobbs, a Montgomery, Alabama, law firm, as bond co-counsel. Andrews saw to the incorporation of the Industrial Development Board of Frisco City and issued an opinion on the legality of the authorization and issuance of the Bonds. Sklar drafted the lease, indenture of trust, mortgage, authorizing resolution, guarantee, and closing papers. The Board entered into a lease with ASECo on November 1, 1972. It required ASECo to pay as base rent the amount necessary to amortize the interest and principal of the Bonds. Harrelson unconditionally guaranteed ASECo's payment of rent under the lease. The Board then adopted the resolution adopting the bond issue. The ability of the Board to meet its financial obligations under the issue depended entirely on ASECo's and Harrelson's financial solvency.

Sklar also drafted the Offering Circular, based on material furnished to him by the underwriter, the lessee

company, and those associated with them, but he intentionally or recklessly disregarded other facts of which he was aware. Sklar omitted from the Offering Circular, for example, that the Securities and Exchange Commission had investigated and commenced a civil action against Hamilton and Investors Associates (and against Jackson Municipals, Inc., the assignee who ultimately underwrote the issue) for violations of the securities laws; he even failed to name the underwriter in the Offering Circular. He misleadingly portrayed ASECo as the owner of 519 acres of Florida real estate valued at $2,284,000, already approved for development, recklessly disregarding not only that ASECo had filed no development plans but also that it had no ownership or equity interest in the property. Although Sklar knew that Harrelson had been only moderately successful at past efforts, he falsely represented Harrelson in the Offering Circular as a successful and experienced developer of modular home manufacturing plans with well-established mobile home sales. Furthermore, Sklar relied on an opinion letter that no actions were pending against or threatening ASECo, even though the opinion letter was

obviously deficient and was prepared by a lawyer other than the one originally selected to give an opinion, as Sklar knew. In fact, an action affecting the Florida investment real estate listed on ASECo's balance sheet was pending at the time of the opinion letter.

Part of the information Sklar incorporated into the Offering Circular was a financial statement prepared by George C. Rakard, a certified public accountant from Salem, Illinois. Rakard's financial statement was materially false and misleading because of numerous misrepresentations and omissions. It included as assets of ASECo a number of items of doubtful worth. Open notes and capital stock subscriptions from Harrelson and his wife were valued at $376,000, in reckless disregard of their true value and without taking into account the Harrelsons' probable inability to satisfy these obligations. Three-quarters of the assets were investment properties, including the Florida real estate in which ASECo in fact had no interest. Moreover, Although Rakard's forwarding letter accompanying the financial statement stated that the audit faily presented the financial condition of ASECo, Rakard knew or recklessly

disregarded the fact that the financial statement constituted mere "window dressing" that did not fairly present ASECo's financial condition.

By the time Sklar incorporated Rakard's financial statement into the Offering Circular, he knew or recklessly disregarded the fact that Harrelson was already in default on at least one of the notes listed as an asset of ASECo and that ASECo was in default on its obligation in the lease to maintain at least $400,000 in working capital.

Meanwhile, Investors Associated had determined that it did not possess sufficient capital to underwrite the proposed issue and assigned the right to underwrite the issue to Jackson Municipals, Inc., a Tennessee underwriting firm headed by Cecil Lamberson. Jackson Municipals and Lamberson proceeded to offer the Bonds for sale to the public on the basis of the Offering Circular, even though they knew it contained materially false misrepresentations and omissions. They knew Harrelson was inexperienced and unsophisticated, contrary to the Offering Circular's representation. They purported to rely on Hamilton and Investors Associates, but because they were all defendants

in the same SEC action (which the Offering Circular failed to disclose) they knew that Investors Associates needed to induce another firm to underwrite the bond issue or it would lose the value of all the time and effort it had put into the issue thus far.

Lamberson and Jackson Municipals knew that while Harrelson was not as financially secure as represented, 95% of ASECo's current assets consisted of open notes from Harrelson and over 75% of ASECo's listed assets was the Florida real estate, but failed to investigate the true value of either of these assets. They knew that the financial statement did not reflect ASECo's true assets. They even failed to inquire whether Harrelson had paid $200,000 due ASECo on a stock subscription, knowing that ASECo would be in default if Harrelson had not. In spite of this knowledge, Jackson Municipals bought the bond issue from the Board in three increments, commencing on December 14, 1972, and resold the Bonds to securities dealers.

The Phenix National Bank (now the First Alabama Bank of Phenix City, NA) had been chosen to act as trustee of the Bond proceeds. The Bank's responsibility was to

ensure that the lessee complied with the terms and conditions of the lease, one of which was that ASECo at all times have working capital in the amount of $400,000.00 or more. The Bank had the duty to determine the existence of any default in the lease requirements by the lessee, and to demand a cure of the default or else declare the Bonds due and payable upon failure to cure. The Bank's responsibility commenced with the sale of the first increment of the Bonds, which took place on December 14,1972. The Bank knew or recklessly disregarded from the date its duties as trustee commenced that ASECo was in breach of the lease requirement that it maintain $400,000.00 in working capital.

The Board entered into an agreement with Coliseum Properties, Inc., to construct part of the facilities contemplated by the bond issue. Coliseum Properties, however, merely served as a vehicle by which substantial parts of the proceeds of the issue were diverted and used for the benefit of others. In particular, the controlling persons of the parent corporation of Coliseum Properties, the so-called "Candler defendants," made improper payments to ASECo and to Harrelson in exchange for the construction contract; more-

over, Coliseum Properties and some of its officers were under indictment in several pending suits. None of this information was known to the Board when it entered into the agreement with Coliseum Properties.

In January 1973, Bishop spoke with his broker, Tom Monks, president of Professional Securities, Inc., a Birmingham securities dealer, about Bishop's investment possibilities. Monks advised Bishop that tax-free Bonds, such as those issued by the Industrial Development Board of the Town of Frisco City, Alabama, were a good investment and he told Bishop of others in the community who had purchased such Bonds.

Bishop purchased three of the Bonds in January, paying $3,052.67, and one more in February, for $1,043.37. The Offering Circular offered the Bonds for sale at 86, that is for $860 per Bond, yet Bishop paid par—$1,000 plus accrued interest for each Bond. The district court found Bishop purchased as part of the primary offering. However, the record does not disclose whether Bishop purchased directly from Jackson Municipals (and, if so, why the price was not as offered), or from his broker acting as principal or

from a seller in the secondary market. Industrial development bonds from towns like Frisco City are not ordinarily traded in a secondary market, but Lamberson stated in deposition that these bonds were being traded, that they were marketable securities, and that his firm had bought and sold some. Indeed, it appears that in addition to its underwriting discount, Jackson Municipals had earned $4,500 by trading these securities in the secondary market. The record is likewise silent as to whether Bishop's purchase was the result of one of these trades .

Bishop never saw the Offering Circular nor knew one existed. He bought the Bonds based solely on his broker's oral representations. At about the same time, he purchased a variety of other municipal bonds offered by various industrial development boards, gas districts, and utility authorities, presumably on similar oral advice from his broker.

After the ASECo plant had been constructed, the lessee ceased all operations at the plant and, on April 15, 1974, defaulted in payment of rent under the lease. Although Harrelson had unconditionally guaranteed the performance of the lease by ASECo, he did not have suffi-

cient assets to back up his guarantee. The Trustee Bank declared the lease in default.

Bishop's original complaint sought relief for himself and for the class of all purchasers of the Bonds under the Securities Act of 1933, 15 *U.S.C. § 77a et seq.*, the Securities Exchange Act of 1934, 15 U.S.C. § 78a *et seq.*, rule 10b-5, 17 C.F.R. § 240.10b-5, and an unspecified Alabama law. The court dismissed all claims under the 1933 Act, which dismissal Bishop does not appeal, but permitted Bishop to amend his complaint twice in order to allege that he relied on the Offering Circular. Bishop's inability to make such an allegation resulted in the dismissal here on appeal.

To the extent that Bishop pleaded the usual 10b-5 misrepresentation or omission case, the district court was correct. Reliance is an essential element of such a cause of action, though the burden of proving or disproving reliance may shift depending on the nature of the case. The elements of a classic mispresentation action are: (1) the defendant must make a false representation of a material fact, (2) knowing its falsity and intending that the plaintiff rely on it, (3) the plaintiff must justifiably rely on it, and (4) suffer

damage as a result. *See* III L. Loss, Securities Regulation 1431 (1961); *Dupuy v. Dupuy, 551* F.2d 1005, 1014 (5th Cir. 1977). Because reliance is so difficult to prove when a defendant has failed to disclose a material fact rather than misrepresenting it, the Supreme Court has allowed the trier of fact to presume reliance in an omission case where the plaintiffs could justifiably expect that the defendants would disclose material information. *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 92 S.Ct. 1456, 31 L.Ed.2d 741 (1972). *Ute* did not eliminate reliance as an element of a 10b-5 omission case; it merely established a presumption that made it possible for the plaintiffs to meet their burden. When the *Ute* presumption attaches, the defendant may rebut it by showing that the plaintiff did not rely on the defendant's duty to disclose. If the plaintiff would have followed the same course of conduct even with full and honest disclosure, then the defendant's action (or lack thereof) cannot be said to have caused plaintiff's loss. *See Simon v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 482 F.2d 880 (5th Cir. 1973), *explained in Rifkin v. Crow*, 574 F.2d 256 (5th Cir. 1978).

Bishop alleged that the Offering Circular contained material misrepresentations and failed to state material facts necessary to make the statements made not misleading. At the same time, he admitted that he never read or otherwise relied on the Offering Circular. If the *Ute* presumption applies to these nondisclosures, Bishop's admission rebuts it. Bishop's claim that he was deceived by the misrepresentations and omissions of the Offering Circular was correctly dismissed by the district court because of his failure to read or even seek to read the Offering Circular.

IV.

The district court erred, however, in construing the remainder of Bishop's complaint as narrowly confined to charges of misrepresentations and omissions in the Offering Circular that would have defrauded investors who did rely. It would permit proof that the defendants engaged in an elaborate scheme to create a bond issue that would appear genuine but was so lacking in basic requirements that the Bonds would never have been approved by the Board nor presented by the underwriters had any one of the

participants in the scheme not acted with intent to defraud or in reckless disregard of whether the other defendants were perpetrating a fraud. Rather than containing the entire fraud, the Offering Circular was assertedly only one step in the course of an elaborate scheme.

Rule 10b-5 provides in part:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, . . .

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Bishop's complaint specifically tracks the language of all three subsections of the rule.[4] As we have stated in Part III, Bishop's 10b-5(2) claim contained in Count I cannot withstand his admitted lack of reliance on the Offering

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[4] In Count I he states;

In connection with the sale of the Bonds, J. C. Harrelson (now deceased) and others, by the use and means of instrumentalities of interstate commerce and the mails, did or caused the following to be done:

> (a) Employed one or more devices, schemes and artifices to defraud Plaintiff and members of the class;
>
> (b) Made to Plaintiff and other members of the class, untrue statements of material fact and omitted to state material facts necessary to be made in order to make the statements made, in the light of the circumstances under which they were made, not misleading in connection with the purchase or sale of the Bonds;
>
> (c) Engaged in acts, practices and courses of business and conduct which operated as a fraud and deceit upon plaintiff and members of the class in connection with the purchase and sale of the Bonds.

In Count II his allegations practically reiterate 10b-5(I) and (3):

In connection with the offer and sale of the bonds, the defendants hereinafter named entered into and participated with J. C. Harrelson in a conspiracy, scheme or agreement to employ devices, schemes and artifices to defraud, and to engage in acts, practices and courses of business which would and did operate as a fraud and deceit upon the Plaintiff and other members of the class sued for herein.

Circular. However, his 10b-5(1) and (3) claims in Counts I and II assert something more that prevents dismissal at this preliminary stage.

Bishop could prove that he made a general request to his broker to purchase industrial development bonds, that his actual purchases covered a number of different issues, and that he did not undertake to determine which among the issues then offered were the most prudent investments or to second-guess the underwriters in the price and coupon rate they set. His pleadings would permit him to show that he was willing to accept any marketable risk. If a municipal authority was willing to authorize the issuance of the Bond, and the underwriters were willing to present the issue to the market, that was sufficient for Bishop's purposes. His pleadings allow him to show that he sought to make investments in securities which were entitled to be marketed.

It is unnecessary here to decide whether a distinction should be drawn between the terms "loss causation" and "transaction causation." *See Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374, 384 (2d Cir. 1974) (Frankel, J., concurring). The concept of this scheme to defraud satisfies

the requirement of "transaction causation." *Id.* at 381; 1 A. Bromberg & L. Lowenfels, Securities Fraud & Commodities Fraud § 4.7 (558)-(559), at 86.25, 86.32 (1979).[5] It has as its core objective that the potential victim engage in the transaction for which the scheme was conceived. The requisite element of causation in fact would be established if Bishop proved the scheme was intended to and did bring the Bonds onto the market fraudulently and proved he relied on the integrity of the offerings of the securities market. His lack of reliance on the Offering Circular, only one component of the overall scheme, is not determinative. *Blackie v. Barrack*, 524 F.2d 891, 906 (9th Cir. 1975).

Bishop has alleged the necessary elements of an action under 10b-5(1) or (3). In the literal words of rule 10b-

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[5] Misrepresentation actions brought under 10b-5(2) may require a separate showing of "transaction causation." In such a case, "the test of 'reliance' is whether 'the misrepresentation is a substantial factor in determining the course of conduct which results in [the recipient's *loss*.'" *List v. Fashion Park, Inc.*, 340 F.2d 457, 462 (2d Cir. 1965) (quoting Restatement, Torts § 546 (1938)). Doing away with the conventional reliance requirement in a 10b-5(2) case, therefore, could establish a scheme of investors' insurance.

5, he must be able to show a "scheme ... to defraud ... or ... [an] act, practice or course of business which operates ... as a fraud or deceit upon [him] ... in connection with the sale of [the Bonds] ...." Bishop's burden of proof will be to show that (1) the defendants knowingly conspired to bring securities onto the market which were not entitled to be marketed, intending to defraud purchasers, (2) Bishop reasonably relied on the Bonds' availability on the market as an indication of their apparent genuineness,[6] and (3) as a result of the scheme to defraud, he suffered a loss.

V.

The thrust of the arguments against our holding is that a recovery in this circumstance is not consonant with

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[6] After *Hochfelder, infra*, this circuit's requirement that the reliance be reasonable or justifiable means only that the plaintiff must not "intentionally refuse[] to investigate 'in disregard of a risk known to him or so obvious that he must be taken to have been aware of it, and so great as to make it highly probable that harm would follow.'"

Dupuy v. Dupuy, *551* F.2d 1005, 1020 (5th Cir. 1977) (quoting W. Prosser, Law of Torts § 34, at 185 (1971)). Defendants do not suggest that a decision to invest in the municipal obligations of Frisco City, Alabama, without more, constitutes an intentional disregard of an obvious risk.

the central purpose of the securities laws, which, it is argued, is to provide full disclosure so that investors may make informed investment decisions. It is asserted that allowing recovery to one who has never read the Offering Circular minimizes the importance of such documents and discourages investors from reading them.[7]

We disagree. First, the purposes of the securities acts and rule 10b-5 are far broader than merely providing full disclosure or fostering informed investment decisions. The Supreme Court has held that the acts were designed "to protect investors against fraud and ... to promote ethical standards of honesty and fair dealing. See H.R. Rep.No. 85,

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[7] This argument ignores § 11 of the Securities Act of 1933, which allows recovery for untrue statements or omissions of a material fact in the registration statement without proof of reliance. Even when the exception in §1 I(a) applies, a plaintiff need not prove that he read the registration statement. Although municipal bonds are exempt from the registration requirements of the 1933 Act, the exemption does not indicate a congressional intent that aggrieved purchasers of municipal bonds must have read an Offering Circular in order to recover. Certainly there are differences between §§11 and 12 of the 1933 Act and § 10(b) of the 1934 Act and rule 10b-5. We point to the former provisions only to indicate that Congress did not have a pervasive intent to require plaintiffs under the securities laws to read or rely specifically on a prospectus or circular.

73d Cong., 1st Sess., 1-5 (1933)." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 195, 96 S.Ct. 1375, 1382, 47 L.Ed.2d 668, 677 (1976). This court has held that "[t]he basic intent of section 10(b) and rule 10b-5 and indeed, of the Exchange Act, is to protect investors and instill confidence in the securities markets by penalizing unfair dealings." *Sargent v. Genesco, Inc.*, 492 F.2d 750, 760 (5th Cir. 1974). *See also Woodward v. Metro Bank of Dallas*, 522 F.2d 84, 91, 93 n.20 (5th Cir. 1975); *Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 495 F.2d 228, 235, 240 (2d Cir. 1974) ("to secure fair dealing"). Thus, the central purpose of the acts is the protection of investors, *Tcherepnin v. Knight*, 389 U.S. 332, 336, 88 S.Ct. 548, 553, 19 L.Ed.2d 564, 569 (1967); *Woodward v. Metro Bank*, 522 F.2d 84, 91 (5th Cir. 1975); *Bellah v. First National Bank, 495* F.2d 1109, 1111 (5th Cir. 1975); *Herpich v. Wallace, 430* F.2d 792, 801, 806-08 (5th Cir. 1970), and the promotion of free and honest securities markets. *Id.* The acts reach complex fraudulent schemes as well as lesser misrepresentations or omissions. Full disclosure is only one means, albeit a central one, of achieving these paramount

goals.[8]

Second, the role of the Offering Circular will continue undiminished even if Bishop proves his allegations and recovers. He has alleged that the fraud caused the Bonds to be offered for sale on the market. If Bishop proves no more than that the bonds would have been offered at a lower price or a higher rate, rather than that they would never have been issued or marketed, he cannot recover. Thus, a purchaser of securities will still have the strongest incentive to read the disclosure statement if he wants to ensure he gets full value for his securities purchases.

Under Bishop's broader theory, it would have availed him nothing to have read the Offering Circular. This theory is not that he bought inferior bonds, but that the Bonds he bought were fraudulently marketed. The securities laws allow an investor to rely on the integrity of the market to the extent that the securities it offers to him for purchase are entitled to be in the market place.

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[8] The schemes must, of course, be one within the "manipulative" condemnation of the securities law. *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 97 S.Ct. 1292, 51 L.Ed.2d 480 (1977). This one clearly is.

Finally, we reject the contention that our holding imposes new burdens on defendants or enhances their liability. Lawyers, underwriters, and accountants who participate in bond issues in good faith are unaffected by our decision. Liability results only if they act with intent to deceive or defraud. None of these parties may be held liable for mere negligent performance of whatever role they choose to play, for the plaintiff must prove that the defendants acted with the requisite scienter. *See Ernst &* Ernst v. Hochfelder, 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976); *Aaron v. SEC*, 446 U.S. 680, 100 S.Ct. 1945, 64 L. Ed 2d 611 (1980). [9]

The dissent asserts that we adopt a "new theory" because we separate Bishop's claim under 10b-5(2) that the Offering Circular was misleading from his claim under 10b-5(1) and (3) that defendants' fraudulently marketed Bonds

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[9] The Court has yet to decide "whether, under some circumstance scienter may also include reckless behavior." *Aaron*, 446 U.S. at 686 n.5, 100 S.Ct. at 1950 n.5. This court has decided that it may. See *Huddleston v. Herman & MocLean*, 640 F.2d 534, 535, 545 (5th Cir. 1981); *Thompson & Co., Inc. v. Partridge*, 636 F.2d 945, 959 (5th Cir. 1981).

caused his loss. It is not our "theory" but the words of rule 10b-5 which confer the right of action we hold Bishop is entitled to try to prove. Contrary to the assertion of the dissent, neither this court nor the Supreme Court has held these parts of the rule do not mean what they say. Misrepresentation and omission cases under 10b-5(2) which, as we do, require reliance on the document making the misrepresentation or omitting a material fact are inapposite to a case in which the buyer relied on the integrity of the market to furnish securities which were not the product of a fraudulent scheme. This circuit has said so,[10] and other circuits have also.[11] There is no Supreme Court precedent to the contrary.

We do not overrule *Rifkin v. Crow*. Rather, we cite it approvingly for the rule 10b-5(2) principle it decides and hold it requires affirmance of the dismissal of that part of Bishop's claim. Moreover, *Rifkin, is* helpful to our holding here in two other respects. It points out that this circuit had

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[10] *Rifkin v. Crow*, 574 F.2d 256 (5th Cir. 1978).

[11] *Blackie v. Barrack*, 524 F.2d 891 (9th Cir. 1975); *Schlick v. Penn Dixie Cement Corp.*, 507 F.2d 374 (2d Cir. 1974).

not previously decided whether a buyer could rely on a "fraud on the market" theory as developed in the Second and Ninth Circuits.[12] *Rifkin* also explains that our prior decision in *Simon v. Merrill Lynch, Pierce, Fenner & Smith,* (holding the lack of "general reliance" on a stockbroker's misrepresentations foreclosed any right of action) would not apply to such a broader theory of fraud if it were developed on remand. "In other words, *Simon's* 'general reliance' language simply requires there to be a causal link between defendant's violation and plaintiff's harm in order for plaintiff to recover." 574 F.2d 262 n.l.

The dissent asserts that *Affiliated Ute Citizens v. United States,* and *List v. Fashion Park, Inc.*, taken together suggest that Bishop's admitted nonreliance on statements or omissions in the Offering Circular precludes any recovery for harm caused by the broader scheme to bring the Bonds onto the market by fraud. We disagree. *Ute* and *List* emphasized that the role of reliance in securities actions is to establish causation. In *Ute,* silence in the face of a duty by

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[12] *See* cases cited in footnote 11, supra.

bank employees to disclose selfdealing established "the requisite element of causation in fact." 406 U.S. at 154, 92 S.Ct. at 1472. Furthermore, *Ute* expressly recognized that rule 10b-5 was not limited to dealing with misrepresentation or omission cases under 10b-5(2), but reached "a 'course of business' or a 'device, scheme or artifice' that operated as a fraud...." 406 U.S. at 153, 92 S.Ct. at 1472. *List* stated that the reason for the reliance requirement "is to certify that the conduct of the defendant actually caused the plaintiff's injury." 340 F.2d at 462. Whenever the rule 10b-5 issue shifts from misrepresentation or omission in a document to fraud on a broader scale, the search for causation must shift also. The "reliance" that produces causation in the latter type of case cannot come from reading a document. It may arise from the duty to speak as in *Ute*, a scheme to manipulate the market at a time when a merger had forced a sale as in *Schlick*, a scheme to inflate common stock prices by misleading statements as in *Rifkin*, or a claim by a bond buyer that he relied on the market to provide securities that were not fraudulently created as we have here. The most significant common thread in all these precedents is that rule 10b-5 is

not limited to a narrow right to recover for knowing fraudulent misrepresentations or omissions in disclosure documents which mislead a securities buyer. The rule is recognized also to provide the basis for a federal cause of action for more elaborate, intentional schemes which deceive or defraud purchasers of securities.

The dissent suggests that our holding needlessly imports a state law cause of action for conversion into the federal securities law. Again we disagree. It is the recognized right of action created by rule 10b-5 which we hold Bishop was denied. This cause of action has its roots in congressional enactment, federal regulation and federal precedent. We merely decline to diminish it.

VII.

The judgment dismissing plaintiff's complaint is vacated and the cause remanded for further proceedings not inconsistent with this opinion. The district court also ruled that this action could not be maintained as a class action because of lack of typicality, lack of adequate representation, and lack of a showing that common questions of fact

would predominate. All three of these determinations, however, were premised on the belief that reliance on the Offering Circular was crucial to Bishop's claim. On remand, the court must reconsider the maintainability of this action as a class action as to members of a properly defined class of Bond purchasers who did not so rely.[13]

VACATED and REMANDED.

* * * * *

RANDALL, Circuit Judge, with whom BROWN, RONEY, GEE, TJOFLAT, JAMES C. HILL, FAY, ALVIN B. RUBIN, REAVLEY and HATCHETT, Circuit Judges, join, dissenting.

The majority opinion today adopts a new theory of recovery in federal court under Rule 10b-5. It holds that a purchaser of securities offered to the public by means of a misleading offering circular, who has heretofore been fore-

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[13] The court previously determined the maintainability of a rule 10b-5(2) class action for Bond buyers who could establish reliance on the Offering Circular. The requirement to reconsider the maintainability of an additional class action does not affect that determination.

closed from recovering in federal court under Rule 10b-5 because of his admitted lack of reliance on the offering circular, will not henceforth be foreclosed from recovering under the Rule if he is able to prove that the defendants knowingly conspired to bring securities onto the market which were not "entitled to be marketed" and that he reasonably relied on the availability of the securities on the market as an indication of their entitlement to be marketed.

This newly-devised route to recovery under Rule 10b-5 is completely without supporting precedent; indeed, it conflicts with the prior decisions of this and every other circuit and with the clear implication of recent Supreme Court decisions in the securities field. But even if the majority were writing on a blank slate, its novel holding would be profoundly unwise for several reasons. First, it introduces into the law under Rule 10b-5 a distinction between securities that are "entitled to be marketed," i. e., securities that may be the subject of a fraudulent marketing scheme, but which, absent the fraud, could be sold at *some* price, and securities that are not "entitled to be marketed." i. e., securities that are the subject of a fraudulent market-

ing scheme and that, absent the fraud, could not be sold at *any* price. The requirements for recovery under Rule 10b-5 in any case hinge upon which category of securities the defrauded plaintiff purchased. If he purchased a security that was entitled to be marketed, he must have relied on the defendants' misrepresentations or omissions in order to recover. If, however, he can show that he purchased a security which was not entitled to be marketed, he can recover in spite of his nonreliance on the defendants' misrepresentations or omissions if he can show that he reasonably relied on the integrity of the marketplace to offer him securities that were entitled to be marketed. This novel theory permits recovery under the Rule to one who has elected not even to seek to read what the seller is obligated by the Rule to disclose, thereby defeating the primary objective of the Rule-the making of an informed investment decision. Second, the majority opinion has great potential for increasing the volume of litigation under Rule 10b-5 by providing a federal forum to those plaintiffs who by their own actions would otherwise have forfeited the protection of the Rule and have relegated themselves to state court

actions for conversion. Finally, the majority opinion also has great potential for protracting much Rule 10b-5 litigation that would heretofore have terminated at the summary judgment stage. For these reasons, I respectfully dissent.

I. THE MAJORITY'S TREATMENT OF THE RELIANCE REQUIREMENT

The majority begins part III of its opinion by acknowledging that reliance is an essential element of a misrepresentation or omission case under section 10(b) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. § 78j(b) (1976). The opinion notes that the trier of fact may presume reliance in an omissions case (as distinguished from a misrepresentations case) in which the plaintiff could justifiably have expected that the defendant would disclose material information. However, that presumption is said by the majority to be rebuttable and is held to have been rebutted in this case by Bishop's admitted failure to read or even seek to read the offering circular.

The majority opinion goes on to distinguish between Bishop's Rule 10b-5(2) case based on misrepresentations and omissions in the offering circular, as to which summary

judgment was proper because of Bishop's admitted lack of reliance on the offering circular, and Bishop's Rule 10b-5(1) and (3) case based upon a scheme to defraud and an act that operates as a fraud, each having as its objective the issue and sale of bonds which were not entitled to be marketed. As to the latter case, lack of reliance by the plaintiff on the offering circular, which is described as "only one component of the overall scheme," is held to be not fatal. Instead, proof of reliance by the plaintiff on the availability of the bonds on the market as an indication that they were entitled to be marketed will suffice.

By way of explanation, the majority opinion tells us that the role of reliance in securities actions is to establish causation, and that whenever the issue under Rule 10b-5 shifts from misrepresentations or omissions in a document to "fraud on a broader scale," the search for causation must also shift. In fraud on a broader scale, the reliance that establishes causation "cannot come from reading a document," but instead can consist of reliance on the market to provide securities that are entitled to be marketed. Thus we are told that we need to view Bishop's case as not simply one

of the class of cases in which the fraud is accomplished by means of misrepresentations and omissions in an offering circular (in which the absence of reliance by the plaintiff on the offering circular would be fatal to the plaintiff's case) but instead as one in a class of cases involving "fraud on a broader scale" or "more elaborate, intentional schemes which deceive or defraud purchasers of securities" (in which the reliance that is needed is simply reliance on the integrity of the market to provide securities that are entitled to be marketed). We are told this in spite of the fact that Bishop's complaint is *accurately* summarized in the opening lines of the majority opinion as alleging "in essence ... that the defendants had fabricated a materially misleading Offering Circular in order to induce the Industrial Development Board ['Board'] to issue, and the public to buy, fraudulently marketed bonds."

The only direct authority cited by the majority for its

novel holding is the Rule itself,[1] which makes it unlawful in connection with the sale of a security to employ any scheme to defraud (clause 1) or to engage in any act which operates as a fraud (clause 3). With deference, I suggest that if it were possible to circumvent the requirement of clause (2) of the Rule of reliance on the defendants' misrepresentations or omissions simply by falling back on the sweeping language of clauses (1) and (3) of the Rule in combination with allegations of elaborate fraud, there would be numerous cases to cite as direct authority for the majority's holding. In fact, there are none.

II. PRIOR PRECEDENT RELATING TO THE RELIANCE REQUIREMENT

A. The Origins and Function of the Reliance Requirement

Perhaps the seminal modern case on the reliance

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[1] In arguing that its holding does not conflict with prior precedent of this circuit or the Supreme Court, the majority virtually concedes that there is no direct *precedential* support for its interpretation of clauses (1) and (3) of the Rule: "It is not our 'theory' but the words of rule 10b-5 which confer the right of action we hold Bishop is entitled to try to prove. Contrary to the assertion of the dessent, neither this court nor the Supreme Court has held [that] these parts of the rule do not mean what they say." *Ante*, 647 F.2d at 471.

requirement *is List v. Fashion Park, Inc.*, 340 F.2d 457 (2nd Cir.), *cert. denied*, 382 U.S. 811, 86 S.Ct. 23, 15 L.Ed.2d 60 (1965). The gravamen of List's complaint was that the defendants had utterly failed to disclose certain material facts, and that as a result thereof, he had lost money in selling securities.[2] The defendants argued that the language of clauses (1) and (2) of Rule 10b—5 could not support liability in a total nondisclosure case, but the Second Circuit firmly rejected the defendants' suggested distinctions that were based on the differing language of the three clauses; instead, the court relied upon the Rule as a whole for its holding that total nondisclosures fell within the ambit of

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[2] In *List*, the plaintiff was an experienced and successful investor who had purchased 5,100 shares of Fashion Park stock in 1959 at $13.50 per share. In November 1960, with the advice of his broker, List authorized the sale of his stock at a net price to him of not less that $18 per share. List's broker knew that at that time, two directors of Fashion Park were bidding for Fashion Park stock through the pink sheets, but the broker did not think it important to disclose this fact to List, and List made no effort to learn whether the directors were in the market for the stock. Another development was the adoption of a resolution by the board of directors of Fashion Park on November 4, 1960, to merge into another company. Fashion Park did not issue a press release about the merger. List sold his stock in mid-November 1960, at $18.50 per share, without knowing that one of Fashion Park's directors was the purchaser or that Fashion Park's management was considering the sale of the company.

Rule 10b—5 and section 10(b). *Id.* at 462. Drawing upon the elements of the common law tort of misrepresentation, the Second Circuit incorporated into the private cause of action under Rule 10b—5 the requirement that the plaintiff have relied upon the defendants' misrepresentations or omissions, even in a total nondisclosure case:

> [T]he test of 'reliance' is whether 'the misrepresentation is a substantial factor in determining the course of conduct which results in [the recipient's] loss.' ... The reason for this requirement ... is to certify that the conduct of the defendant actually caused the plaintiff's injury ....
>
> This interpretation of Rule 10b—5 is a reasonable one, for the aim of the rule in cases such as this is to qualify, as between insiders and outsiders, the doctrine of *caveat emptor*—not to establish a scheme of investors' insurance. Assuredly, to abandon the requirement of reliance would be to facilitate outsiders' proof of insiders' fraud, and to that extent the interpretation for which plaintiff contends might advance the purposes of Rule 10b—5. But this strikes

> us as an inadequate reason for reading out of the rule so basic an element of tort law as the principle of causation in fact.

Id. at 462-63 (bracketed portion inserted by Second Circuit). In applying this principle to the case before it, the Second Circuit held that the trial court's detailed findings of fact, to the effect that List would have sold his stock even had he been aware of the undisclosed information, were not clearly erroneous; accordingly, the showing of causation necessary to support a private recovery under Rule 10b—5 was missing, and List could not recover.

This court promptly adopted the rule of *List. E. g., Herpich v. Wallace,* 430 F.2d 792, 805 & n.12 (5th Cir. 1970) (citing *List); Crumbles v. Times Herald Printing Co.,* 387 F.2d 593 (5th Cir.), *cert. denied,* 390 U.S. 1028, 88 S.Ct. 1419, 20 L.Ed.2d 285 (1968) (affirming per curiam a judgment for defendant on basis of adequately supported jury findings that plaintiff did not rely and that omitted facts were not material).

B. Modifications to the Manner in Which the Reliance Requirement May Be Satisfied

Subsequent to the *List* decision, the federal courts have developed two modifications in the manner in which reliance may be established, both of which are aimed at overcoming what would otherwise be virtually insurmountable obstacles for plaintiffs. The first modification applies only to nondisclosure cases—i.e., those cases in which the defendants have remained silent in the face of a duty to disclose. The second modifications applies only to certain "fraud on the market" claims—typically class actions in which a great many plaintiffs have allegedly suffered losses in the secondary trading market as a result of misrepresentations or omissions in a series of documents promulgated by the defendants over a period of time.

1. The rebuttable presumption of reliance in total nondisclosure cases.—In many instances, the violation of Rule 10b—5 complained of by the plaintiff is a total failure to disclose material information, as was true in *List*. Early in the 1970s' the federal courts increasingly became aware that in such total nondisclosure cases, a plaintiff faces almost an insurmountable burden if he is required to present affirmative evidence that he relied specifically on the

defendants' silence with regard to a material fact.

The Supreme Court first addressed this problem in Affiliated *Ute Citizens v. United States,* 406 U.S. 128, 92 S.Ct. 1456, 31 L.Ed.2d 741 (1972). The defendants in *Affiliated Ute,* who were marketmakers in the stock of a company holding assets for certain Indians, as well as sales agents for the Indians, had remained silent as to prevailing market prices for the stock in circumstances in which they had a duty to disclose those prices. The Indians "considered these defendants to be familiar with the market for the shares of stock and *relied upon them* when they desired to sell their shares." *Id.* at 152, 92 S.Ct. at 1471 (emphasis added). [3] The Supreme Court held that the Tenth Circuit had erred when it held that there was no violation of the Rule unless the record disclosed evidence of reliance on material fact misrepresentations by [the defendants]. We do not read Rule 10b—5 so restrictively. *To be sure, the second sub-paragraph of the rule specifies the making of a untrue statement of a*

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[3] *See also Chiarella v. United States,* 445 U.S. 222, 229—30, 100 S.Ct. 1108, 1115, 63 L.Ed.2d 348 (1980) (including, in a description *of Affiliated Ute,* a reference to the reliance by the Indian sellers upon the Bank's personnel).

material fact and the omission to state a material fact. The first and third subparagraphs are not so restricted. These defendants' activities, outlined above, disclose within the very language of one or the other of those subparagraphs, a "course of business" or a "device, scheme, or artifice" that operated as a fraud upon the Indian sellers. *Superintendent of Insurance v. Bankers Life & Casualty Co.*, [404 U.S. 6, 92 S.Ct. 165, 30 L.Ed.2d 128] (1971)].... The sellers had the right to know that the defendants were in a position to gain financially from their sales and that their shares were selling for a higher price in that market ....

> *Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery.* All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision .... This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact.

Id. at 152-54, 92 S.Ct. at 1471-1472 (emphasis added; some

citation omitted).

The courts of appeals have not read *Affiliated Ute* as having done away with the reliance requirement altogether. Rather, *Affiliated Ute* has been read to establish a rebuttable presumption what the plaintiff relied upon the defendant's silence in total nondisclosure cases, at least so long as the facts as to which the defendants were silent meet the materiality requirement. For example, in *Rifkin v. Crow*, 574 F.2d 256 (5th Cir. 1978), the law in this circuit on reliance was carefully summarized and restated, with special attention paid to *Affiliated Ute:*

> After *Ute*, the reliance requirement has varied somewhat in articulation from circuit to circuit, but a general pattern seems to have emerged: where a 10b—5 action alleges defendant made positive misrepresentations of material information, proof of reliance by the plaintiff upon the misrepresentation is required. Upon an absence of proof on the issue, plaintiff loses. On the other hand, where a plaintiff alleges deception by defendant's nondisclosure of material information, the *Ute* presumption obviates

> the need for plaintiff to prove actual reliance on the omitted information. Upon a failure of proof on the issue, defendant loses. But this presumption of reliance in nondisclosure cases is not conclusive. *If defendant can prove that plaintiff did not rely, that is, that plaintiff's decision would not have been affected even if defendant had disclosed the omitted facts, then plaintiff's recovery is barred.*

Id. at 262-63 (footnotes omitted). *Accord, Huddleston v. Herman & MacLean, 640* F.2d 534, 547-50 (5th Cir. 1981) ("reliance is an issue in *all* Rule 10b—5 cases"); *Dwoskin v. Rollins, Inc.*, 634 F.2d 285, 291 n.4 (5th Cir. 1981); *Moody v. Bache & Co.*, 570 F.2d 523, 528 (5th Cir. 1978); *Vohs v. Dickson*, 495 F.2d 607, 622 (5th Cir. 1974); *Rochez Brothers, Inc. v. Rhoades*, 491 F.2d 402, 410 (3d Cir. 1974); *Simon v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 482 F.2d 880, 884-85 (5th Cir. 1973). Indeed, until today, this circuit has uniformly required not only that there have been reliance (whether established by means of an unrebutted presumption under *Affiliated Ute* or proved directly by the plaintiff),

but also that the plaintiff's reliance have been *reasonable.*"[4]

The majority opinion does not purport to overrule any of these cases. Indeed, it specifically disclaims any intent to overrule *Rifkin by* treating it as a case arising only

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[4] Judge John Minor Wisdom, writing for our court in *Dupuy v. Dupuy, 551 F.2d 1005* (5th Cir.) *cert. denied,* 434 U.S. 911, 98 S.Ct. 312, 54 L.Ed.2d 197 (1977), summarized the elements of a private cause of action under Rule 10b—5:

> The courts have established that with regard to private recovery for the violation of rule 10b—5, a properly stated cause of action must establish the scienter of the defendant, the materiality of any misrepresentation or omission by the defendant, the *extent of actual reliance* by *the plaintiff on the defendant's statements, and the justifiability of the reliance,* frequently translated into a requirement of due diligence by the plaintiff.

Id. at 1014 (emphasis added; footnotes omitted). The argument made in *Dupuy* was that because *Ernst & Ernst v. Hockfelder,* 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976), required that the plaintiff prove scienter as part of his cause of action, the plaintiff's lack of diligence in investigating the information available to him should not defeat recovery because the defendant's culpability would be of a far greater degree. The *Dupuy* court rejected this argument, however:

> [T]o abandon completely the consideration of reliance in fact and reasonable reliance ignores not only the above-stated policies of due diligence but also the need for a causal link between the misrepresentation or omission and the injury suffered by the private plaintiff. The cause of action would no longer provide compensation for losses occasioned by the violation of the [1934] Act because a plaintiff could sue without relying on the fraud. This would transform the action into an enforcement mechanism. We reject this approach ....

under clause (2) of Rule 10b—5. Admittedly, the opinion in *Rifkin* does not make an explicit distinction between cases

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Id. at 1016. The court did agree, however, that *Hockfelder* called for a modification of the standard of care under which the plaintiff's conduct would be judged—i.e., a modification that would broaden the definition of "reasonable" reliance. Backing away somewhat from our previous definition of reasonableness, as expressed in cases such as Clement A. Evans & Co. v. McAlpine, 434 F.2d 100, 103-04 (5th Cir. 1970). cert. denied, 402 U.S. 988, 91 S.Ct. 1660, 29 L.Ed.2d 153 (1971), the *Dupuy* court held that mere negligence was not enough to make the reliance unreasonable; instead, to defeat recovery on grounds that the plaintiff's reliance was unreasonable, the plaintiff's conduct must have been a refusal to investigate in disregard of a risk known to him or so obvious that he must be taken to have been aware of it, and so great as to make it highly probable that harm would follow. 551 F.2d at 1020.

This court has steadfastly adhered to *Dupuy's* requirement that the plaintiff's reliance have been reasonable—i.e., within the standard of care articulated by the *Dupuy* court. See, e. g., Paul F. Newton & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1121-22 (5th Cir. 1980) (Charles Clark, J.); Swenson v. Engelstad, 626 F.2d 421, 424 (5th Cir. 1980).

The majority points out that there has been no allegation in this case that Bishop lacked due diligence. Ante, 647 F.2d at 470 n.6. But since there was positive proof of Bishop's nonreliance, there is simply no issue as to the reasonableness of Bishop's reliance.

Nonetheless, *Dupuy* and its progeny are extremely relevant to our inquiry: Judge Wisdom's reasoning, in rejecting the argument that the reasonableness of the plaintiff's reliance should not be a part of his cause of action, is equally applicable in this case, where the majority dispenses not with the requirement that the plaintiff's reliance be reasonable, but with the more fundamental requirement that he have relied in the first place.

arising under clause (2) of the Rule and those arising under clauses (1) and (3). But *Rifkin* does make a clear distinction between misrepresentation and omission cases, and its holding as to the latter is premised on Affiliated Ute (which was itself a holding under clauses (1) and (3)). This leads me to believe that in *Rifkin* and its progeny this court has spoken to the question of whether proof of nonreliance bars recovery in a case arising under clauses (1) and (3)—and has held that it does. *Huddleston v. Herman & MacLean, supra,* reads *Rifkin* in this manner.

Further, the majority opinion squarely conflicts with the decision of the Eighth Circuit in *Vervaecke v. Chiles, Heider & Co.*, 578 F.2d 713 (8th Cir. 1978). Although the majority chooses not to discuss *Vervaecke*, that case also involved an initial public offering of bonds and featured a plaintiff who, by his own admission, had not relied on a defective offering circular. Sensing that his admission might be fatal to a clause (2) claim, he urged that his case should be considered as one involving primarily nondisclosure cognizable under clauses (1) and (3) of Rule 10b—5. The Eighth Circuit specifically declined to do so and held instead

that the district court had properly granted summary judgment for the defendants because of the plaintiff's admitted nonreliance on the offering circular.

Regardless of whether the majority opinion conflicts directly or only indirectly with the cases discussed above. it is clear at least that *none* of these prior cases dealing with the reliance requirement even indirectly supports the majority's holding today. If those cases are not explicitly overruled, I believe that for the reasons expressed below in part III, their practical vitality has been emasculated *sub silentio* by the majority.

2. Reliance in "fraud on the market" class actions.— In insisting that it is not overruling *Rifkin v. Crow,* the majority notes in part VI of its opinion that *Rifkin* "points out that this circuit *had not previously* decided whether a buyer could rely on a 'fraud on the market' theory as developed in the Second and Ninth Circuits"[5] In an accompanying footnote, the majority cites *Schlick v. Penn-Dixie*

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[5] *Ante,* 647 F.2d at 471 & n.12. Rifkin lists a number of "fraud on the market" cases in addition to *Blackie. See* 574 F.2d at 263 n.4.

Cement Corp., 507 F.2d 374 (2d Cir. 1974), *cert. denied*, 421 U.S. 976, 95 S.Ct. 1976, 44 L.Ed.2d 467 (1975), and *Blackie v. Barrack*, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816, 97 S.Ct. 57, 50 L.Ed.2d 75 (1976). *Schlick is* not a "fraud on the market" case in the usual sense of that term, but as discussed below in part II—C, it represents another sort of modification to the reliance requirement. *Blackie*, however, is the seminal and best known of the "fraud on the market" cases. Earlier, in part IV of its opinion, the majority cites *Blackie* for the proposition that Bishop's "lack of reliance on the Offering Circular, only one component of the overall scheme, is not determinative."[6] The inference is that the majority believes that *Blackie* and the other "fraud on the market" cases support its holding in the case at bar.

Blackie is typical of the "fraud on the market" cases in that it involved an extremely large class of plaintiffs who purchased the securities of an issuer at different times over an extended period. The gravamen of the claims of all members of the putative class was the alleged misrepresen-

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[6] *Ante*, 647 F.2d at 469.

tation by the issuer of its true financial condition in annual and interim reports, press releases, and SEC filings. One ground upon which the defendants resisted the named plaintiffs' motion for class certification was that the need for direct proof of subjective reliance by each class member would inevitably create sufficient conflicts between class members and the named plaintiffs as to make the named plaintiffs' representation inadequate.

The Ninth Circuit recognized that it was virtually impossible in the context of classwide proceedings for each class member to present direct proof of his subjective reliance.[7] The court therefore established a rebuttable presumption for those cases alleging deception that inflated the price of stock traded on the open market:

> [P]roof of subjective reliance on particular misrepresentations is unnecessary to establish a 10b—5 claim for a deception inflating the price of stock traded in the open market. Proof of reliance is adduced to

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[7] *Cf. Huddleston v. Herman ~ MacLean*, 640 F.2d 534, 549 (5th Cir. 1981) ("in a class action, while the materiality element can be established for the class as a whole, reliance, like damages, is a matter of individual proof").

> demonstrate the causal connection between the defendant's wrongdoing and the plaintiff's loss. We think causation is adequately established in the impersonal stock exchange context by proof of purchase and of the materiality of misrepresentations, without direct proof of reliance. Materiality circumtantially establishes the reliance of some market traders and hence the inflation in the stock price—when the purchase is made the causational chain between defendant's conduct and plaintiff's loss is sufficiently established to make out a prima facie case.

Id. at 906 (citations omitted). Drawing upon a distinction made by the Second Circuit in *Schlick* between "loss causation" and "transaction causation," the Ninth Circuit specifically rejected the notion that a Rule 10b—5 action can be predicated solely on a showing of loss causation:

> The 10b—5 action remain.s compensatory; it is not predicated solely on a showing of economic damage (loss causation). We merely recognize that individual "transactional causation" can in these circum-

> stances be inferred from the materiality of the misrepresentation, *see Tucker v. Arthur Andersen & Co.*, [67 F.R.D. 468, 480 (S.D.N.Y. 1975)]; *Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374, 381—382 (2d Cir. 1974), and shift to defendant the burden of disproving a prima facie case of causation. Defendants may do so in at least 2 ways: 1) by disproving materiality or by proving that, despite materiality, an insufficient number of traders relied to inflate the price; and 2) *by proving that an individual plaintiff purchased despite knowledge of the falsity of a representation, or that he would have, had he known of it.*

Id. (footnote omitted; emphasis added).

Blackie's significance to the case at bar rests in its holding that despite a presumption of reliance in "fraud on the market" cases, the defendant may still defeat recovery by positive proof of nonreliance. The Ninth Circuit has consistently adhered to this rule. E. g., *Keirnan v. Homeland, Inc.*, 611 F.2d 785, 788-89 (9th Cir. 1980). Thus, *Blackie* provides absolutely no support for the majority's partial abandonment of the reliance requirement .

C. The Limited Circumstances in Which Reliance May Be Unnecessary

My own research reveals only one factual situation in which the reliance requirement arguably would be unjustified. That situation was presented in *Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374 (2d Cir. 1974), *cert. denied*, 421 U.S. 976, 97 S.Ct. 57, 50 L.Ed.2d 75 (1975)—a case cited by the majority in connection with a distinction between "loss causation" and "transaction causation."[8]

Schlick did not allege fraud resulting in his purchase of a security; instead, he alleged that a fraudulent proxy statement was one step in a scheme that led to the forced liquidation of his security.[9] The Second Circuit noted that

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[8] Ante, 647 F.2d at 469.

[9] Plaintiff Schlick was a minority shareholder in Continental Steel; defendant Penn-Dixie had become a majority shareholder in Continental and thus had voting control. Schlick alleged that Penn-Dixie, by causing Continental's assets to be used for its own purposes, artificially depressed the market price of Continental stock and inflated the market price of Penn-Dixie stock. Schlick alleged that, as part of a scheme, Penn-Dixie proposed to merge Continental into a Penn-Dixie subsidiary but failed to disclose in a proxy statement issued before the merger the manner in which Penn-Dixie had inflated the value of its shares at the expense of Continental. Penn-Dixie then merged Continental into a subsidiary, with the result that the minority shareholders in Continental received an unfairly low exchange ratio.

this was *not* a typical Rule 10b—5 case:

> This is not a case where the 10b-5 claim is based solely upon material omissions or misstatements in the proxy materials. Were it so, concededly there would have to be a showing of both *loss causation*—the misrepresentations or omissions caused the economic harm—and *transaction causation*—that the violations in question caused the appellant to engage in the transaction in question. The former is demonstrated rather easily by proof of some form of economic damage, here the

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Significantly, Continental's minority shareholders had no power to prevent the merger. Under state law a majority of the outstanding shares was all that was required in order to effect the merger. The exchange of the Continental shares held by Schlick and the other minority shareholders for those of the Penn-Dixie subsidiary was, effectively, a forced sale in which they made no investment decision. Schlick's class action, which was founded upon sections 10(b) and 14(a) of the 1934 Act, and Rules 10b-5 and 14a-9 thereunder, was dismissed by the district court on the ground that it failed to present any allegation of injury which was *caused* by the allegedly false and misleading proxy statement other than that caused by the unfair merger itself. After reviewing the allegations of the complaint and the decision of the district court, the Second Circuit noted that the nature of the fraud alleged in the complaint—engagement in a course of business which operated as a fraud and deceit on the purchasers and holders of Continental stock—was encompassed by clause (3) of Rule 10b-5.

> unfair exchange ratio, which arguably would have been fairer had the basis for valuation been disclosed. Transaction causation requires substantially more.

507 F.2d at 380 (emphasis in original; footnote omitted). The court went on to explain the two ways in which a plaintiff could make a prima facie showing of transaction causation:

> In a misrepresentation case, to show transaction causation a plaintiff must demonstrate that he relied on the misrepresentations in question when he entered into the transaction which caused him harm.... In an omission or nondisclosure case based upon Rule 10b-5, a plaintiff need not show reliance in order to show transaction causation but must still show that the facts in question were material "in the sense that a reasonable investigator might have considered them important" in making his investment decisions.

Id. As an exception to the general proposition that a plaintiff must allege and prove transaction causation to recover under Rule 10b-5, the court carved out a limited exception:

> Under the 10b-5 count, *proof of transaction causation is unnecessary by virtue of the allegations as to the effectuation of a scheme to defraud which includes market manipulation and a merger on preferential terms,* of which the proxy omissions and misrepresentations are only one aspect. Thus appellant need only show loss causation with respect to his claim for relief under 10b-5; [the court below] found and we agree that this has been shown. Here the complaint clearly alleges that, as *a result of the merger, appellant was forced to sell* his Continental shares to Penn-Dixie on the basis of an exchange ratio that reflected adversely the manipulated market value of Continental stock, and that he sustained injury accordingly.

Id. at 381 (emphasis added).

Schlick, then did not even arguably fit within clause (2) of Rule 10b-5. The misrepresentations and omissions in the proxy statement did not cause the plaintiff's loss. Instead, the claim involved, to paraphrase the Second Circuit's opinion, a forced sale in

which the plaintiff had no opportunity to make an *investment decision* and in which, therefore, the defendants' misrepresentations and omissions in, the proxy statement were not the sole mechanism—or even the *key* mechanism—through which the fraudulent scheme was to be accomplished. The object of the scheme was not to induce the minority stockholders to make an erroneous decision based on the misstatements and omissions in the proxy statement, for their decision on the proxy solicitation was irrelevant to the success of the scheme; rather, those misstatements and omissions were part of the alleged plan to cover up the essence of the fraud, which was the manipulation of stock prices to set the scene for an unfair exchange ratio in a forced merger. Transaction causation was irrelevant because the minority shareholders were not called upon to make an investment decision. The specific holding of the *Schlick* case, then, can be summarized as follows: when a plaintiff alleges that he has sustained a loss as the result of a fraudulent scheme to bring about a

forced sale of his security, he need not plead or prove transaction causation (including reliance, actual or presumed) because he has made no investment decision to participate in the transaction. *Accord, Crane Co. v. Westinghouse Air Brake Co.*, 419 F.2d 787, 797 (2d Cir. 1969), *cert. denied*, 400 U.S. 822, 91 S.Ct. 41, 27 L.Ed.2d 50 (1970) ("where the success of a fraud does not require an exercise of volition by the plaintiff, but instead requires an exercise of volition by other persons, there need be no showing that the plaintiff himself relied upon the deception"); *Vine v. Beneficial Finance Co.*, 374 F.2d 627, 635 (2d Cir.), *cert. denied*, 389 U.S. 970, 88 S.Ct. 463, 19 L.Ed.2d 460 (1967) ("[whatever need there may be to show reliance in other situations [citing *List* and other cases], we regard it as unnecessary in the limited instance when no volitional act is required and the result of a forced sale is exactly that intended by the wrongdoer").

Though the specific holding in *Schlick* obviously is inapplicable given the facts of the case at bar, the portion of

the Second Circuit's opinion dealing with loss causation and transaction causation is instructive. Ours is a case in which, to quote the majority opinion, "the complaint alleged that the defendants had fabricated a materially misleading Offering Circular in order to induce the Industrial Revenue Board to issue, and the public to buy, fraudulently marketed bonds."[10] Whether this case is viewed as a misrepresentations case or an omissions case,[11] the named plaintiff and every member of the putative class voluntarily entered into the transaction as the result of an investment decision. If we adhere to *Schlick*, each must show transaction causation—including reliance (actual or presumed) on the offering circular. In this case the existence of reliance has been definitively disproved by Bishop's admission that he did not

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[10] *Ante*, 647 F.2d at 464 (footnote and bracketed definition of terms omitted).

[11] In my view, this is primarily a misrepresentations case rather than an omissions case because the defendants undertook to sell the bonds pursuant to an offering circular. *See Huddleston v. Herman & MacLean*, 640 F.2d *534*, 548 (5th Cir. 1981) ["t]his case, involving alleged misstatements and omissions in a prospectus published pursuant to a public offering, cannot properly be characterized as an omissions case of the type for which the *Affiliated Ute* presumption was fashioned"); *Vervaecke v. Chiles, Heider & Co.*, 578 F.2d 713 717 n. 2, 718 & n. 4 (8th Cir. 1978).

read or even seek to read the offering circular. And, as the majority opinion correct concludes, presumptive reliance has been rebutted by the same admission.

In short, neither *Schlick, Blackie,* nor any other case cited by the majority supports its holding. In fact, the majority's holding runs contrary to the clear implication of every case from this circuit and others in which the reliance requirement has been considered.

III. REASONS FOR ADHERENCE TO THE RELIANCE REQUIREMENT

A. The Policy Behind the Reliance Requirement

In the case at bar, the majority holds that nonreliance on the defendants' misrepresentations or omissions is not fatal to some cases brought under clauses (1) and (3) of Rule 10b-5 and creates instead a new sort of reliance requirement for those cases—reliance on the integrity of the marketplace. Other than the majority's interpretation of the policies and the congressional purpose behind the federal

securities laws,[12] there is absolutely no support for the majority's holding today in the prior precedent of this or any other court.

In part V of its opinion, the majority correctly states that "[t[he thrust of the arguments against [its] holding is that a recovery in this circumstance is not consonant with the central purpose of the securities laws, which, it is argued, is to provide full disclosure so that investors may

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[12] Justice Rehnquist's opinion in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 95 S.CT. 1917, 44 L.Ed.2d 539 (1975), emphasizes the importance of weighing competing policy concerns:

> [W]e would by no means be understood as suggesting that we are able to divine from the language of § 10(b) the express "intent of Congress" as to the contours of a private cause of action under Rule 10b-5. When we deal with private actions under Rule l0b-5, we deal with a judicial oak which has grown from little more than a legislative acorn. Such growth may be quite consistent with the congressional enactment and with the role of the federal judiciary in interpreting it, . . . but it would be disingenuous to suggest that either Congress in 1934 or the Securities and Exchange Commission in 1942 foreordained the present state of the law with respect to Rule l0b-5. It is therefore proper that we consider . . . what may be described as policy considerations when we come to flesh out the portions of the law with respect to which neither the congressional enactment nor the administrative regulations offer conclusive guidance.

Id. at 737, 95 S.Ct. at 1926.

make informed investment decisions."[13] The majority then cites phrases from a number of cases[14] for the proposition that "[f]ull disclosure is only one means, albeit a central one,

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[13] *Ante*, 647 F.2d at 470; MS at 16.

[14] The complete quote from *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976), reads as follows:

> The Securities Act of 1933 (1933 Act), 48 Stat. 74, as amended, 15 U.S.C. § 77a *et seq.*, was designed to provide investors with full disclosure of material information concerning public offerings of securities in commerce, to protect investors against fraud and, through the imposition of specified civil liabilities, to promote ethical standards of honesty and fair dealing. See H.R.Rep.No.85, 73d Cong., 1st Sess., 1-5 (1933). The 1934 Act was intended principally to protect investors against manipulation of stock prices through regulation of transactions upon securities exchanges and in over-the-counter markets, and to impose regular reporting requirements on companies whose stock is listed on national securities exchanges. See S.Rep.No. 792, 73d Cong., 2d Sess., 1-5 (1934).

Id. at 195, 96 S.Ct. at 1382. Even more informative is the actual language from *Tcherepnin v. Knight*, 389 U.S. 332, 88 S.Ct. 548, 19 L.Ed.2d 564 (1967):

> The Securities Exchange Act [of 1934] quite clearly falls into the category of remedial legislation. One of its central purposes is to protect investors *through the requirement of full disclosure by issuers of securities*, and the definition of security in § 3(a)(10) necessarily determines the classes of investments and investors which will receive the Act's protections.

of achieving [the] paramount goals" of the federal securities laws.[15] I disagree.

This court recognized over a decade ago that in the context of a private suit for damages,

> the sweeping language of Rule 10b-5 creates an almost completely undefined liability. All that the rule requires for its violation is that someone "do

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Id. at 336, 88 S.Ct. at 553 (emphasis added; footnote omitted). The majority also cites *Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 495 F.2d 228 (2d Cir. 1974), but that case says:

> As we have stated time and again, the purpose behind Section 10(b) and Rule 10b-5 is to protect the investing public and to secure fair dealing in the securities markets *by promoting full disclosure of inside information so that an informed judgment can be made by all investors who trade in such markets.*

Id. at 235 (emphasis added). And in *Herpich v. Wallace*, 430 F.2d 792 (5th Cir. 1970), we described Congress' intent as follows:

> In short, *Congress meant to afford investors a reasonable opportunity to make knowing, intelligent decisions regarding their purchases and sales of securities in unmanipulated markets,* . . . and the loss resulting in connection with purchases or sales made without benefit of such an opportunity is the type of injury section 10(b) and Rule 10b-5 seek to prevent.

Id. at 806 (emphasis added).

[15] *Ante*, 647 F.2d at 471.

> something bad" in connection with a purchase or sale of securities. Without further delineation, civil liability is formless, and the area of proscribed activity could become so great that the beneficial aspects of the rule would not warrant the proscription. In recognition of this problem, courts have sought to construct workable limits to liability under section 10(b) and Rule 10b-5 which will accommodate the interests of investors, the business community, and the public generally.

Herpich v. Wallace, 430 F.2d 792, 804-05 (5th Cir. 1970) (citations omitted). In an accompanying footnote, id. at 805 n.12, we listed the reliance requirement first among the court-made limits on civil liability under Rule 10b-5. Citing our decision in *Herpich,* with approval, the *Blue Chip Stamps* Court shared our "concern that the inexorable broadening of the class of plaintiffs who may sue in this area of the law will ultimately result in more harm than good." 421 U.S. at 747-48, 95 S.Ct. at 1931.

The Supreme Court and this court have recognized that there must be limits in defining the class of persons who

may recover under Rule 10b-5. The policy question presented by the case at bar is whether the traditional reliance requirement is a sensible limit in *all* cases in which the plaintiff has made an investment decision. I believe that this question must be answered in the affirmative .

The reliance requirement promotes the objectives of the 1934 Act by precluding recovery to a plaintiff who has made an investment decision by his own lights and without reference to the information promulgated under the disclosure requirements of the federal securities laws. Whether disclosure is viewed as a goal or as a mechanism to achieve a goal, it is crucial to the way in which the federal securities laws function. Just as the threat of litigation and massive liability under Rule 10b-5 is intended to deter fraudulent conduct connected with the purchase or sale of a security, the reliance requirement is intended to encourage investors to base their investment decisions on information required by the securities laws to be disclosed. In short, the federal securities laws are intended to put investors into a position from which they can help themselves by relying upon disclosures that others are obligated to make. This system

is not furthered by allowing monetary recovery to those who refuse to look out for themselves. If we say that a plaintiff may recover in some circumstances even though he did not read and rely on the defendants' public disclosures, then no one need pay attention to those disclosures and the method employed by Congress to achieve the objective of the 1934 Act is defeated. Indeed, after reading the offering circular in this case and considering the disclosures about the weak and highly questionable financial position of ASECo that *were* made therein, I am left with the nagging question of whether Bishop would have had a loss if he had read the offering circular, latently defective as it may have been.[16]

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[16] The inadvisability of taking any action that would have the effect of minimizing or eliminating the need to read the offering circular is highlighted by the facts of this case. The offering circular may well have contained the latent material misrepresentations and omissions described at great length and in detail in the plaintiff's second amended complaint. But if the plaintiff or someone acting for the plaintiff (such as the broker form whom he bought the bonds, who is not a defendant in this case) had read the offering circular, the disclosures that are made in the financial statements included therein might very will have warned him of the risk inherent in the bonds and of the calibre of the people involved in the transaction pursuant to which the bonds were issued.

The second paragraph of the accountant's report on the financial statements of ASECo, Inc. as of August 31, 1972, reveals

Apart from the fact that the reliance requirement makes sense in the context of the objectives of the 1934 Act and the method chosen by Congress to achieve those objectives, there is another reason for not eliminating the reliance requirement in a suit under Rule 10b-5. To paraphrase Justice Stewart's opinion in *Aaron v. SEC,* 446 U.S. 680,

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on its facethat the accompanying financial statements were *not* prepared in accordance with generally accepted accounting principles:

> Investment real estate having a net book value of $473,436.66 is carried on the enclosed balance sheet at $2,420,500, an increase for statement purposes of $1,947,063.34. One parcel is supported by an appraisal dated October 12, 1971, by a member of the American Institute of Real Estate Appraisers at a value of $2,284,000.

The significance of the increase in the carrying value of the real estate "for statement purposes" in the amount of $1,947,063.34 becomes clear when we turn to the balance sheet, where the net worth of ASECo, Inc. is shown as $2,203,657.33. If we subtract from that net worth the amount wrongly included in it ($1,947,063.34), we are left with a net worth of $256,593.99. If we examine that number more closely, we find that it is based in part on three items (totaling $430,787.05) included in Current Assets under thc heading "Advances to Stockholders"—one item in the amount of $176,091.40 called "Open Notes," a second item in the amount of $54,695.65 called "Used for purchase of corporate shares for company account," and a third item in the amount of $200,000.00 called "Capital Stock subscriptions receivable." The footnote to the "Open Notes" item contains the following piece of information: "Stockholders propose to liquidate a portion of these advances by assigning to the corporation their equity in residence real estate, valued at $77,000.00." The footnote to the "Used for

689, 100 S.Ct. 1945, 1951, 64 L.Ed.2d 611 (1980), we do not write on a blank slate in determining whether reliance is a necessary element for recovery under section 10(b) and Rule 10b-5. The basic requirements of a cause of action under Rule 10b-5 (which are listed in part III of the majority opinion) have remained largely intact since the Rule was adopted. The Supreme Court has consistently turned back efforts to

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purchase of corporate shares for company account" item contains this description of the transaction involved: "The stockholders obtained funds for the purpose of purchasing certain common stocks for the account of the company. We were advised that the shares have been forwarded to the registrars for registration in the company's name." Finally, the footnote to the "Capital Stock subscriptions receivable" item contains the following information: "The company is holding a note from J. C. Harrelson in which he has promised to purchase 1667 shares of capital stock in the company within sixty days of August 31, 1972."

All three of the items listed in current assets under the heading "Advances to Stockholders" would have to be viewed with *great* skepticism, particularly in view of their materiality, individually and in the aggregate, to the financial statements. And, if they are eliminated from current assets, ASECo, Inc. is insolvent.

In summary, the accountant's report included in the offering circular is irregular on its face; the financial statements included therein are highly questionable on their face and strongly suggest that ASECo, Inc. was insolvent or nearly so on the balance sheet date. The average investor in industrial revenue bonds, when presented with the accountant's report and financial statements for ASECo, Inc. would, in my view, have had a good indication that the entire transaction was questionable and extremely risky.

eliminate or water down those requirements. E. *g.*, *Santa Fe Industries, Inc. v. Green, supra* (only conduct involving manipulation or deception is reached by section 10(b) or Rule 10b-5; private action under Rule 10b-5 will not lie for mere abuse of fiduciary duty); *Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976) (private cause of action for damages will not lie under section 10(b) and Rule 10b-5 in the absence of any allegation of scienter; allegation of negligence insufficient); *Blue Chip Stamps v. Manor Drug Stores, supra* (private damages action under Rule 10b-5 is confined to actual purchasers or sellers of securities).[17] *Cf. Aaron v. SEC, supra* (SEC is required to establish scienter as an element of a civil enforcement

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[17] Indeed, of late the Court has shown marked reluctance to extend the contours of private causes of action under the securities laws generally. *E. g., Transamerica Mortgage Advisors, Inc. v. Lewis,* 444 U.S. 11, 100 S.Ct. 242, 62 L.Ed.2d 146 (1979)(no implied private right of action under § 206 of Investment Advisers Act of 1940); *Touche Ross & Co. v. Redington,* 442 U.S. 560, 99 S.Ct. 2479, 61 L.Ed.2d 82 (1979) (no implied private right of action under § 17(a) of 1934 Act); *Piper v. Chris-Craft Industries, Inc.,* 430 U.S. 1, 97 S.Ct. 926, 51 L.Ed.2d 124 (1977)(no implied private right of action under §14(e) of 1934 Act; unsuccessful tender offeror lacked standing to sue for damages under Rule 10b-6); *TSC*

action to enjoin violations of section 10(b) and Rule 10b-5); *Chiarella v. United States*, *445* U.S. 222, 100 S.Ct. 1108, 63 L.Ed.2d 348 (1980) (recognizing that while silence in connection with purchase or sale of securities may operate as a fraud actionable under Rule 10b-5(1) and (3), criminal liability must be premised on duty to disclose arising from relationship of trust and confidence between parties to a transaction). We do not have a license to do what the Supreme court has refused to do.

B. The Majority's "Fraud on a Broader Scale" Exception to the Reliance Requirement

The majority opinion containes two conflicting views of the nature of this case. The opening lines of the majority opinion describe the plaintiff's complaint as alleging "in essence . . . that the defendants had fabricated a materially misleading Offering Circular in order to induce the Indus-

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Industries, Inc. v. Northway, Inc., 426 U.S. 438, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976) (rejecting Seventh Circuit's expansive definition of materiality in private suits under Rule 14a-9 as encompassing "all facts which a reasonable investor might consider important"; misstatement or omission in proxy solicitation is material only if there is "substantial likelihood" that a reasonable shareholder *would* (not "might") consider the fact important in deciding how to vote).

trial Development Board . . . to issue, and the public to buy, fraudulently marketed bonds."[18] But elsewhere in the opinion, the offering circular is described as "only one component of the overall scheme."[19] Following the latter view of the case, the majority opinion states that "[w]henever the rule 10b-5 issue shifts from misrepresentation or omission in a document to fraud on a broader scale, the search for causation must shift also. The 'reliance' that produces causation in the latter type of case cannot come from reading a document. It may arise from . . . a claim by a bond buyer that he relied on the market to provide securities that were not fraudulently created. . . ."[20] The conflicts in the majority opinion suggest the question: What kind of a case do we really have here?

The answer to that question is clear to me. The majority opinion had it right the first time. We have a case in which the fraud on the plaintiff and the other purchasers

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[18] *Ante*, 647 F.2d at 464.

[19] *Ante*, 647 F.2d at 469.

[20] *Ante*, 647 F.2d at 472.

of the bonds was effected by means of a misleading offering circular. The defendants are the participants in that offering—the underwriters who sold the bonds, the lawyers who participated in the preparation of the offering circular, the accounting firm that rendered a report on the financial statements included in the offering circular, the bank that acted as a trustee under the mortgage securing the bonds, and various persons who are alleged to have aided and abetted the issuer of the bonds and controlling persons of the issuer. While the plaintiff's second amended complaint chronicles at length and in detail the manner in which the proceeds of the bonds were allegedly dissipated or diverted, the essence of the fraud insofar as the plaintiff and other bond purchasers are concerned consisted of the sale of bonds to the public by means of a misleading offering circular. The "shift" in the Rule 10b-5 issue described in the majority opinion to "fraud on a broader scale" is a shift effected by the majority in order to avoid the result otherwise mandated by the application to this case of the traditional elements of a private cause of action under Rule 10b-5. The majority's only justification for the shift is that Bishop's complaint, like all

Rule 10b-5 complaints, tracks the language of the entire Rule and urges the applicablity of clauses (1) and (3).[21]

The majority correctly makes the point that the Rule is not limited to a narrow right to recover for knowing fraudulent misrepresentations or omissions in disclosure documents. It goes on to say that the Rule (meaning, presumably, clauses (1) and (3) of the Rule) is "recognized" to provide the basis for a federal cause of action for "fraud on a broader scale" or "more elaborate, intentional schemes which deceive or defraud purchasers of securities."[22] That statement is wrong. No other court has applied clause (1) or (3) of the Rule on the basis of the scale or elaborateness of the scheme to defruad. As the very cases cited by the majority demonstrate, clauses (1) and (3) of the Rule have been applied instead to cases in which the fraud is not covered by clause (2) of the Rule—i. e., to total omissions cases, such as

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[21] It does not appear that Bishop argued *any* of the majority's theories—his entitlement to rely on the integrity of the market, the bonds' lack of entitlement to be marketed, or the fraud on a broader scale—in the district court. These theories are not mentioned at all in the district court's memorandum opinion.

[22] *Ante*, 647 F 2d at 472.

Ute, or to cases, such as *Schlick,* in which the fraud is accomplished by means of what the defendants did *(e.* g., manipulated the market) rather than by means of what they said.[23]

To permit the plaintiff in a case clearly covered by clause (2) of the Rule to fall back on the broad language of clause (1) (which reaches schemes to defraud) or clause (3) (which reaches acts that operate as a fraud), in combination with allegations of elaborate collateral conduct, in order to

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[23] One leading commentary on the securities laws suggests that a distinction should be drawn between those situations in which the defendants themselves did something to the plaintiff and those situations in which the defendants induced the plaintiff to do something by means of a misrepresentation or omission of a material fact:

> Where the gravamen of the action is something other than misrepresentation or non-disclosure, then of course the question of reliance does not arise. For example, if the complaint is that the defendant sold $5,000,000 of securities belonging to the corporation and pocketed the proceeds, or used them to pay for a controlling block of the corporation's stock, as in *Superintendent of Insurance v. Bankers Life & Casualty Co.,* 404 U.S. 6, 92 S.Ct. 165, 30 L.Ed.2d 128 (1971)], it makes no sense to ask whether anyone relied upon anything. *The complaint is about what the defendant did, not what he said or didn't say.*

R. Jennings & H. Marsh, Securities Regulation: Cases and Materials 1064 (4th ed. 1977) (emphasis added). This distinction is in accord with my discussion of the *Schlick* case in part II-C above.

obviate the effect of the failure to comply with the reliance requirement under clause (2), makes the reliance requirement of clause (2) a dead letter in the one situation in which it most typically applies—the offering of a security, pursuant to an offering circular, to investors who are called upon to make routine investment decisions. The majority notes in footnote 5 of its opinion that to do away with the reliance requirement in a Rule 10b-5(2) case could establish a scheme of investors' insurance, which numerous courts have held was not the intent of section 10(b). Yet, given the scienter requirement, it is difficult to conceive of conduct actionable under clause (2) of Rule 10b-5 that is not also actionable under the broader language of clauses (1) and (3). The majority's holding threatens to turn all of Rule 10b-5 into a scheme of investor's insurance—at least where the security offered can be shown to be not "entitled to be marketed"—and it does so in what is, insofar as the plaintiff is concerned, an ordinary transaction flowing from his voluntary investment decision to purchase a security.

In my view, clauses (1) and (3) of the Rule were drafted broadly so as to reach fraudulent behavior by defen-

dants that is not covered by the literal language of clause (2). But clauses (1) and (3) should not be used, as they are by the majority, to obviate for a plaintiff any of the traditional proof requirements of a cause of action under clause (2).

The majority opinion is a harginger of difficulties for future securities litigation. Surely ingenious plaintiffs' counsel will hereafter plead the "entitled to be marketed/ fraud on a broader scale" theory at least as an alternative basis for recovery. The question whether a security was "entitled to be marketed," i. e., whether the security, absent the fraud, could have been sold at some price, and the question whether the scale of the fraud was broad enough, are both presumably questions of fact, not readily disposed of by summary judgment. The creation of this new recovery theory will not only breed more litigation, but it will also make that litigation more difficult and time consuming. Whether the end result will by any different can be determined only be seers.

The length to which the majority goes to preserve a remedy in federal court for Bishop suggests that Bishop and others like him who did not rely on the offering circular

might otherwise be without a remedy. In fact, if what he alleges in his complaint is true, Bishop had a remedy under Rule 10b-5 against his broker, upon whom he did rely and who advised him that the bonds were a good investment. He chose, for reasons known only to him, not to sue his broker. Surely his election not to sue the person against whom he had a legitimate Rule 10b-5 claim and instead to sue those against whom recovery under Rule 10b-5 has heretofore been precluded should not result in this court's fashioning new law for his benefit. Further, the scheme to defraud that Bishop describes clearly constitutes common law conversion and would be actionable in state court. There is, therefore, no necessity in this case to create a new route to recovery under Rule 10b-5 in order to provide a remedy in federal court for Bishop and others like him who, by their own actions, have forfeited the protection of the Rule.

For the foregoing reasons, I would affirm the decision of the district court granting summary judgment in favor of the defendants.

APPENDIX F

No. 81-839. Jerald H. Sklar, Et al., Petitioners v. James L. Shores, Jr., Executor or the Estate of Clarence E. Bishop, Jr.

459 US 1102, 74 L.Ed. 2d 949, 103 S.Ct. 722

January 10, 1983. Petition for writ of certiorari to the Untied States Court of Apeals for the Fifth Circuit denied.

Same case below, 647 F2d 462, CCH Fed Secur L Rep ¶ 98033.

APPENDIX G

IN THE UNITED STATES DISTRICT COURT FOR THE
NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

JAMES L. SHORES, as Executor of the Estate of Clarence E. Bishop, Jr., on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Industrial Board of the Town of Frisco City, Alabama,	)	
Plaintiffs,	)	
	)	CIVIL ACTION NO. 75-G-618-S
JERALD H. SKLAR; et al.,	)	
Defendants.	)	

ORDER

In conformity with and pursuant to the memorandum opinion entered contemporaneously herewith, it is

ORDERED, ADJUDGED and DECREED that the motion filed by Norman Habshey for leave to intervene in the above-styled action be and it hereby is DENIED; and it is

FURTHER ORDERED that neither Norman

Habshey nor James L. Shores is an adequate class representative and that, no one else having come forward as a potential party-class representative, plaintiff's motion to certify this action as a class action is due to be and the same hereby is DENIED.

It is FURTHER ORDERED that this cause proceed to trial on the individual federal securities law claims asserted by plaintiff James L. Shores, as executor of the estate of Clarence E. Bishop, Jr. All other claims, including the class claims asserted by plaintiff James L. Shores, are hereby DISMISSED.

It is FURTHER ORDERED that the memorandum of decision and order of this court dated August 2, 1977, be and it hereby is RE-ADOPTED except insofar as it relates to the class claim and as to issues of intervention as discussed in the memorandum opinion entered contemporaneously herewith.

DONE and ORDERED this 30th day of July 1986.

/s/ J. Foy Guin, Jr.
UNITED STATES DISTRICT JUDGE
J. FOY GUIN, JR.

IN THE UNITED STATES DISTRICT COURT FOR THE
NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

JAMES L. SHORES, as Executor of the Estate of Clarence E. Bishop, Jr., on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Industrial Board of the Town of Frisco City, Alabama,	)	
Plaintiffs,	)	
v.	)	CIVIL ACTION
	)	NO. 75-G-618-S
JERALD H. SKLAR; et al.,	)	
Defendants.	)	

MEMORANDUM OPINION

Pursuant to orders entered April 15, 1985, and July 9, 1985, this cause came on for an evidentiary hearing August 29, 1985, on the issues embodied in the May 20, 1983, motion of plaintiff to certify this action as a class action under Rule 23(b)(3), Federal Rules of Civil Procedure, and the April 25, 1984, motion of Norman Habshey for leave to intervene as a plaintiff. The factual and procedural

background of this action is generally reflected in the August 2, 1977, Memorandum of Decision of this court, the May 26, 1981, en banc decision of the Fifth Circuit Court of Appeals, 647 F.2d 462 (cert. denied 459 U.S. 1102 (1983)), and the matters filed in this court since the mandate from the Fifth Circuit Court of Appeals was received February 16, 1983.

At the August 29, 1985, evidentiary hearing the court gave the attorneys for plaintiff and for movant-intervenor Habshey the opportunity to present all evidence they desired to offer, subject to the opportunity to supplement their presentation with testimony (and additional documents) from a custodian of certain records held by First Alabama Bank of Phenix City, N.A., described in a subpoena received in evidence as plaintiff's Exhibit 4 and subject also to the opportunity to offer evidence in rebuttal to evidence to be offered by defendants. With one immaterial exception, defendants did not have the opportunity to present their direct evidence at the August 29, 1985, hearing, as the hearing was recessed to accommodate a conflicting court hearing in which counsel for plaintiff was engaged.

The attorneys were directed to submit written memoranda by September 18, 1985, on the admissibility of certain evidence offered by plaintiff at the August 29, 1985, hearing, with the evidentiary hearing to resume on September 23, 1985. At the September 23, 1985, hearing the court gave all parties the opportunity to present all evidence they desired to offer on the class action issue and on the intervention issue, following which hearing the parties rested. The additional briefing period has expired and the issues are ripe for decision.

Following receipt of the mandate in this court on February 16, 1983, the court conducted on June 2, 1983, a pretrial conference to determine the precise claims and issues remaining for resolution in this action. The court invited briefs from counsel on what claims and issues remained. It was not until the receipt of the briefs ordered by the April 15, 1985, order that briefs responsive to that invitation have been received. At the commencement of the August 29, 1985, evidentiary hearing the court advised counsel that it would proceed to delineate those claims and issues.

In its May 26, 1981 en banc decision the Fifth Circuit Court of Appeals vacated this court's final judgment of August 2, 1977, and directed this court on remand to "reconsider the maintainability of this action as a class action as to members of a properly defined class of bond purchasers who did not so rely." 647 F.2d at 472.

After a careful review of this court's August 2, 1977, Memorandum of Decision and the May 26, 1981, en banc decision of the Fifth Circuit Court of Appeals, this court is satisfied that the claims and issues currently in this action which need to be addressed differently from the manner addressed by the August 2, 1977, Memorandum of Decision are:

(1) the individual federal securities law claim of James L. Shores, as Executor of the Estate of Clarence E. Bishop, under Section 10b-5(1) and (3) based upon the defendants knowingly conspiring to bring securities onto the market which were not entitled to be marketed, intending to defraud purchasers; and

(2) the Rule 23, Federal Rules of Civil Procedure, issues associated with Shores's effort to pursue that claim for and on behalf of all bond purchasers with a similar claim and who, like

Bishop, did not rely on the Offering Circular.

Based upon the August 2, 1977, Memorandum of Decision and this court's conclusion of the effect thereon of the May 26, 1981, en banc decision, this court intends to enter an order contemporaneously herewith dismissing all claims other than the individual and class federal securities law claims of Shores described above. Based on the discussion below, this court's order will also dismiss the class claims of plaintiff.

The remaining issues presently before the court are the ones to which the evidentiary hearings of August 29, 1985, and September 23, 1985, were addressed; namely whether Norman Habshey should be permitted to intervene and, assuming his intervention is permitted, whether he may be certified as a class representative, and in any event whether Shores may be certified as a class representative. The court is of the opinion that Habshey should not be permitted to intervene and is further of the opinion that if he were to be permitted to intervene he would not be an appropriate class representative. The court is further of the opinion that Shores would not be an appropriate class

representative. No one else having come forward as a potential party-class representative, class certification will be denied.

Habshey's motion to intervene clearly is untimely. Furthermore, his claims are barred by the applicable statutes of limitation. Habshey was aware of the default on the Frisco City bonds and of the pending lawsuit, at least by the year 1975. During the eight years that follow acquisition of that knowledge, the mandate of the court's order dated August 1, 1977 (permitting intervention within six months), was not followed and Habshey's claims were extinguished by the bar of the statute of limitations. Habshey did not move for intervention until April 25, 1984, some nine years after the suit was filed and almost seven years after this court's order of August 1, 1977.

Without being permitted to intervene, obviously Habshey cannot be a class representative. However, even if the court is in error in determining Habshey's intervention to be untimely, he would nevertheless be unqualified to act as a class representative in this case. The discussion of this proposition hereinafter is merely an alternative holding as

to Habshey on the class representative issue. By no means does the court mean to dignify Habshey's position as even being arguably sound, since he cannot even make an arguably sound argument for intervention.

Habshey's testimony at the hearing confirmed defendants' contentions that he would not be an adequate class representative. His testimony totally lacks credibility, and the court would never certify as a class representative a witness whom it simply could not believe. Habshey's demonstrated lack of credibility would "cast a shadow" over the class claims, and his demonstrably contradictory testimony would be a major focus at trial. Such considerations require a refusal of certification. Kline v. Wolf, 702 F.?_d 400 (2d Cir. 1983); Panzirer v. Wolf, 663 F.2d 365 (2d Cir. 1981); Darvin v. International Harvester Co., 610 F. Supp. 255 (S.D.N.Y. 1985).

Habshey repeatedly and without explanation contradicted his deposition testimony of July 2, 1985, providing conflicting testimony on important points. For example, in his deposition Habshey described several times his conversation with Bill Monks shortly after the bonds' default at

which time Monks told Habshey about this suit. Habshey elaborated upon the reasons for his lengthy delay in intervening. Astonishingly, at the hearing Habshey claimed Monks did not tell him about the litigation and that he did not find out about it until 1983. Ultimately, Habshey acknowledged that Monks "might have told me that," but denied any present recollection.

Habshey also gave contradictory testimony about this post-default conversation with Tom Monks. In his deposition Habshey testified that he called Tom Monks and "raised Hell." At the hearing, Habshey first denied recalling such a conversation with Tom Monks, then, inexplicably, Habshey testified as to the content of the conversation.

Conversely, Habshey's memory concerning his receipt of the 1980 distribution by the Trustee improved dramatically following his deposition. On deposition Habshey maintained that he had no recollection at all of obtaining a check for his bonds. At the hearing, however, Habshey remembered receiving the check, and claimed that its receipt instigated his mention of the bonds to his attorney-nephew some three years later.

Habshey claimed that his deposition testimony stating that he read an attorney's opinion on these bonds was incorrect. His contention that he bought the bonds because they were "marketable" was undercut by his testimony that Tom Monks induced his purchase by falsely representing that the Bonds were "A" rated and approved by the Alabama Securities Commission.

Habshey lacks the basic understanding of the claims and parties necessary for him to supervise the conduct of this suit. See Greenspan v. Brassler, 78 F.R.D. 130 (S.D.N.Y. 1978); Darvin v. International Harvester Co., 610 F. Supp. 255 (S.D.N.Y. 1985).

Even though defendants, by their briefs, alerted Habshey's attorney prior to the hearing that his lack of knowledge could be fatal, Habshey professed total ignorance. He was unable correctly to identify a single one of the numerous defendants, or to recall anything about the nature of the claims asserted by plaintiff. Habshey admitted that he intends to leave the conduct of the suit entirely up to his attorney, abdicating all responsibilities of class representation.

The typicality issue is presented in an unusual fashion in this case. Because the plaintiff has presented no information as to the circumstances of any putative class member's purchase (other than Habshey) the court cannot know what the actual claims of putative class members might be. Therefore, it is difficult to say what claims would be typical of the unknown buyer's circumstances.

The hearing demonstrated, however, that neither Shores's nor Habshey's position is typical of the claims alleged in the latest complaint. A putative representative's claims are not typical if his legal or factual position is markedly different from those he would represent or if determination of class claims might turn in large part on individual factual determinations. See 7 C. Wright and A. Miller, Federal Practice and Procedure, § 1764 (1985 Supp.); McNichols v. Loeb, Rhoades & Co., 97 F.R.D. 331 (N.D. Ill. 1982).

Shores failed to establish typicality at the class action hearing. As he conceded, due to the deaths of both Bishop and Monks, Shores has no means available to prove what Bishop's claims might have been. Therefore, he could

not establish that Bishop's claims were typical. As the owner of potential rights that cannot be proved, Shores occupies a unique position.

Norman Habshey's testimony confirmed defendants' contention that his claims are untypical. Habshey repeated his claims that Tom Monks represented that the bonds were "A" rated and approved by the Alabama Securities Commission, and that he would not have purchased but for these misrepresentations. Habshey also testified that the main factor in this purchase was his mistaken belief that the bonds were backed by the full faith and credit of Frisco City. Habshey also explained that when he testified that he relied upon the "marketability" of the bonds he meant the "soundness of the city" that he thought was backing the bonds. Furthermore, Habshey paid par for his bonds. This was not typical. The Offering Circular priced the bonds at 86.

Regardless of its truthfulness or not, Habshey's testimony exposes him to personal defenses of nonreliance upon the market, which render his claims untypical. Case law holds that such a purchaser cannot properly be certified as a class representative in a fraud-on-the-market suit. See

McNichols v. Loeb, Rhodes & Co., 79 F.R.D. 331 (N.D. Ill. 1982); Markewich v. Ersek, 98 F.R.D. 9 (S.D.N.Y. 1982).

The Court of Appeals' opinion precludes the certification of any class the identity of whose members functionally could not be ascertained. The court's instruction that the district court should consider the maintainability of the class of purchasers who did not rely upon the Offering Circular would require this court before certification of a class to conduct individual adjudication and fact finding merely to determine who would be in the class. Such individual adjudication would violate all principles of Rule 23, Federal Rules of Civil Procedure. At the class certification hearing, plaintiff was not able to bring forward any evidence, inferences or suggestions that would assist the court in overcoming this insurmountable obstacle.

Additionally, Plaintiff could not establish numerosity. Even after the hearing, this court has no evidence whatsoever that if a class of purchasers who did not rely upon the Offering Circular exists, its members would be sufficient in number to justify class action treatment. Plaintiff's attorneys devoted much of their efforts at the

hearing to documenting the number of holders of the bonds at certain dates. Plaintiff's counsel made no attempt at all to show that the holders were also purchasers; plaintiff obviously did not try to show that any of the holders were purchasers who did not rely on the Offering Circular. The only evidence adduced at the hearing on this point came from the deposition of Cecil Lamberson, a principal of the underwriter of this bond issue. Defendants offered Lamberson's testimony that he distributed the Offering Circular widely, sending one to everyone who ordered a bond from his firm.

Thus, the court has no evidence before it that would suggest the existence of a sufficiently numerous class of purchasers who did not rely upon the Offering Circular. The only evidence before the court contradicts a suggestion that such a class would be numerous. James L. Shores, Jr., and Norman Habshey are not adequate class representatives, and their alleged claims are not typical. Neither Shores nor Habshey bolstered his case for appointment as a class representative by his testimony at the hearing.

Shores's testimony confirmed that Shores has no

means to prove Bishop's case, much less to prove the class claims. Shores admitted at the hearing that he has no personal knowledge of the circumstances of Bishop's purchase, and he knows of no one else who does. This unique weakness of Shores's case makes him an inadequate class representative.

Furthermore, that testimony showed that the basis upon which Shores, as executor, is prosecuting this suit is questionable and fraught with conflict of interest. The Bishop estate, which has a presumable claim of approximately $2,600.00 plus possible interest, is risking a much greater sum in costs and expenses. The propriety of Mr. Shores, as executor, risking the estate's assets (if any) in such a venture is dubious. Clarence Bishop's will specifically directed Shores, as executor, "to divide and without order of Court and by property instrument convey all property belonging to my estate as soon as he may deem necessary, but in no event shall the division date be later than six months from the date of my death."

Norman Habshey's testimony at the hearing confirmed defendants' prehearing contention that he is not an

adequate class representative, and his claims are not typical of the alleged class claims.

Clarence E. Bishop, Jr., filed this suit purporting to sue on behalf of a class of bond purchasers. On appeal the Fifth Circuit narrowed the putative class to those purchasers who did not rely on the Offering Circular. See 647 F.2d at 472. The plaintiff and his counsel apparently have never acknowledged the Court of Appeals' narrowing of the putative class. To the contrary, Shores now boldly seeks to broaden the class definition, claiming that it should include "all persons who ever held the Frisco City Bonds."

Ignoring the putative class suggested by the Court of Appeals, the plaintiff attempted to prove the numerosity of holders of the bonds. The plaintiff's effort falls two levels short of relevance. The plaintiff has not even proved the number of purchasers, much less the number of purchasers who did not rely on the Offering Circular. In addition to his failure to address the putative class in this case, plaintiff's attempt to base a class on the number of holders of bonds overlooked the fundamental distinction in federal securities law between holders and purchasers.

In Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 95 S. Ct. 1917, 44 L. Ed. 2d 539 (1975), the Supreme Court held that only purchasers or sellers of securities can state a claim under Rule 10b-5. Holders of securities, as such, have no cause of action. Plaintiff's contention is based upon the mistaken assumption that persons who "received bonds by operation of law are properly within the plaintiff class." In Rose v. Arkansas Valley Environmental & Utility Authority, 562 F. Supp. 1180, 118890 (W.D. Mo. 1983) (another dispute initiated by Clarence Bishop), the court expressly rejected a similar plaintiffs' contention. The court there held that three nonpurchasing holders of securities could not recover under Section 10(b) of the Securities Exchange Act of 1934. Two of the three holders had inherited bonds and the third was the trustee of an inter vivos trust to which a deceased purchaser had given bonds. Applying Blue Chip, the court noted that the holders' predecessors may have been defrauded, but "any cause of action which might thereby have been created was personal to those predecessors; it did not inure in or automatically follow the security itself." 562 F. Supp. at 1189.

Accordingly, under Blue Chip, holders of securities, as such, have no cause of action and plaintiff's effort to equate holders and purchasers was misinformed.[1] Plaintiff did not offer evidence of numerosity of any class of purchasers. He assuredly offered no evidence to demonstrate that the putative class suggested by the Court of Appeals would be numerous. The only evidence in the record implies that numerosity is not present. Determining the adequacy of putative class representatives is a matter committed to the sound discretion of the trial court. The burden of proof rests with the putative class representative. See Susman v. Lincoln

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[1] Plaintiff's reliance upon In re U. S. Financial Securities Litigation, 69 F.R.D. 24 (S.D. Cal. 1975), was misplaced. That case does not stand for the proposition that holders who are not purchasers can be class members. The specific class definition in that case was as follows:

> This action is designated as a class action on behalf of all holders of 9% Bearer Debentures due April 1, 1982 of U. S. Financial Overseas, N.V., guaranteed by U. S. Financial, Incorporated, who also purchased said debentures between April 8, 1970 and July 23, 1973, inclusive.

69 F.R.D. at 55. While the court did not specifically address the Blue Chip decision, which apparently was announced after In re U. S. Financial was taken under submission, the court's definition of the class made certain that all members were purchasers of the subject securities.

American Corp., 561 F.2d 86, 90 (7th Cir. 1977). Plaintiff James L. Shores, Jr., cannot establish the most fundamental requirement of class representation—membership in the class. See Johnson v. American Credit Co., 581 F.2d 526, 532 (5th Cir. 1978). Shores is not a purchaser of the bonds and did not suffer any injury as a result of the actions alleged in the complaint.

Moreover, Shores has conceded his inability to bring forward any evidence as to the circumstances of his testator's purchase. He has admitted that he neither has personal knowledge nor knows of anyone else still alive who does. Both Clarence Bishop and his seller, Tom Monks, are dead. Accordingly, Shores lacks the means to establish that Bishop would be in the putative class of purchasers who did not rely on the Offering Circular.

Shores is unable to establish membership in the putative class either on behalf of himself or his testator. Shores did not suffer the same alleged injuries as the putative class, and he has no ability even to prove his own testator's case. Manifestly, Shores is in no position to "stand in judgment" for the class.

Antagonism or conflict of interest between class members and the putative representative may require disqualification of a proposed class representative. Horton v. Goose Creek Independent School District, 690 F.2d 470 (5th Cir. 1982). Clarence Bishop's will, which was received into evidence, imposed upon Shores, his executor, duties that conflict with the responsibilities Shores proposes to undertake in this case. Item Three of the will stated:

> I hereby constitute and appoint James L. Shores, Jr., as the Executor of this my Last Will and Testament, and hereby direct that as such he shall not be required to give bond or to file an inventory of my estate in any Court.
>
> I hereby empower my said Executor to divide and without order of Court and by property instrument convey all property belonging to my estate as soon as he may deem necessary, but in no event shall the division date be later than six months from the date of my death.

The will obviously presents Mr. Shores with a conflict of interest. The will commanded Bishop's executor to distribute all estate property within six months of Bishop's death. However, if Shores fulfilled Bishop's directions and closed the estate, he could not prosecute this lawsuit.

Defendants argue other considerations, but it is

already clear that the application for class certification is fatally flawed both on grounds of lack of numerosity and lack of typicality, in addition to the other problems already discussed.

Shores has attempted to bolster his position by offering in evidence the answers to interrogatories filed by Mr. Bishop when he was alive and the only plaintiff in the case. These answers are plainly hearsay and inadmissible. They fall within none of the stated exceptions to the hearsay rule. Plaintiff relies upon the 1970 case of Treharne v. Callahan, 426 F.2d 58 (3d Cir. 1970), decided before enactment of the Federal Rules of Evidence. That case held that Rules 26(d), 33 and 43(a) of the Federal Rules of Civil Procedure accorded interrogatory answers the same status as deposition testimony. The circuit court affirmed the district court's order admitting the answers of a deceased defendant, holding that the matter was discretionary with the trial judge.

Treharne is obsolete, due to the 1970 and 1975 revisions of the Rules of Civil Procedure and the adoption of the Federal Rules of Evidence. Prior to 1970, Rule 33,

Federal Rules of Civil Procedure, provided that answers to interrogatories "may be used to the same extent as provided in Rule 26(d) for the use of the deposition of a party." The 1970 amendments to the Federal Rules, however, repealed this foundation for the Treharne analysis, separating interrogatories from the rule under which depositions are admissible. The new rule, which is now in effect, provides, in part, that "the answers may be used to the extent permitted by the rules of evidence." Rule 33(b), Federal Rules of Civil Procedure.

The advisory committee proposed this change in the admissibility of interrogatory answers because of its conviction that interrogatories were not apposite to depositions due to the absence of cross-examination, stating:

> The use of answers to interrogatories at trial is made subject to the rules of evidence. The provisions governing use of depositions, to which Rule 33 presently refers, are not entirely apposite to answers to interrogatories, since deposition practice contemplates that all parties will ordinarily participate through cross-examination.

Advisory Committee Note, 48 F.R.D. 487, 524 (1969). As noted by the Virginia Law Review, "[t]he change implicitly

overrules Treharne's admission of the answers." Note, "Dead Men Tell No Tales: Admissibility of Civil Depositions upon Failure of CrossExaminations," 65 Va. L. Rev. 153, 167, n. 72 (1979).

The new Rule 33, coupled with the 1975 revision of Rule 43(a) and the enactment of the Federal Rules of Evidence, places the analysis for admissibility of interrogatory answers squarely and exclusively under the Federal Rules of Evidence. The legal and analytical bases of Treharne have been repealed.

The Treharne court also, in part, rested its decision on Rule 43(a) of the Federal Rules of Civil Procedure, which at the time governed the admission of evidence in the federal district courts. Although Rule 43(a) was substantially modified when the Federal Rules of Evidence were enacted, at the time of the Treharne decision that rule allowed for admission of evidence which was admissible under the statutes of the United States, under the rules of evidence previously applied in federal courts sitting in equity, or under the rules of evidence applied in the courts of general jurisdiction of the state in which the federal court is held.

Rule 43(a) was construed to follow the most lenient of the three sources of evidence law stated in the rule. The Third Circuit acknowledged that the evidence would not have been admissible under a statute of the United States or the law of Pennsylvania, but admitted the evidence under the theory that it would have been admissible in a federal court sitting in equity. The court stressed that its holding was limited to an interpretation of Rule 43:

> We emphasize that all we decide is that Rule 43 permits the use here of the established equity rule that in the case of death of a witness prior to crossexamination the district judge is permitted to exercise discretion as to whether to admit the testimony given.

426 F.2d at 63.

Rule 43(a) no longer exists in the form necessary to uphold Treharne. It now reads as follows:

> In all trials the testimony of witnesses shall be taken orally in open court, unless otherwise provided by an Act of Congress or by these rules, the Federal Rules of Evidence, or other rules adopted by the Supreme Court.

The reference to the evidence admissible in courts of equity essential to the Treharne holding has been completely deleted.

Class certification is denied. The petition of Habshey to intervene is denied. An order consistent herewith will be entered.

This case will be set on a pretrial docket November 25 or 26 of this year, and a trial date will be scheduled at that time.

DONE this 30th day of July 1986.

/s/ J. Foy Guin,Jr.
UNITED STATES DISTRIC JUDGE
J. FOY GUIN, JR.

IN THE UNITED STATES COURT OF APPEALS

FOR THE ELEVENTH CIRCUIT

NO. 86-7898

JAMES L. SHORES, JR., Executor of the Estate of Clarence E. Bishop, Jr., on behalf of himself and all other persons who purchased First Mortgage 3% Revenue Bonds issued by the Industrial Board of the Town of Frisco City, Alabama,

Plaintiff-Appellant,

versus

JERALD H. SKLAR, et al.,

Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Alabama

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Before HILL, JOHNSON and CLARK, Circuit Judges

BY THE COURT:

Appellees' motion to dismiss Habshey's appeal is CARRIED WITH THE CASE.

Habshey's motion for sanctions is DENIED.

Appellees' motion to dismiss Shores's appeal is DENIED. See Love v. Turlington, 733 F.2d 1562 (11th Cir. 1984).

Shores's motion for sanctions is DENIED.

APPENDIX H

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 86-7898

JAMES L. SHORES, JR., Executor of the Estate of Clarence E. Bishop, Jr., in behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Industrial Board of the Town of Frisco City, Alabama,

Plaintiff-Appellant,

versus

JERALD H. SKLAR, ET AL.,

Defendants-Appellees.

Appeal from the United States District Court
for the Northern District of Alabama

(May 10, 1988)

Before FAY and KRAVITCH, Circuit Judges, and ATKINS*, Senior District Judge.

KRAVITCH, Circuit Judge:

*Honorable C. Clyde Atkins, Senior U. S. District Judge for the Southern District of Florida, sitting by designation.

On this appeal we revisit the case that established the "fraud on the market" theory of securities law in our

predecessor circuit. See Shores v. Sklar, 647 F.2d 462 (5th Cir. May 1981) (en banc), cert. denied, 459 U.S. 1102 (1982) (Shores I).[1]

I.

The events giving rise to this litigation occurred almost sixteen years ago. In 1972, J.C. Harrelson, the president of Alabama Supply & Equipment Co. (ASECo) decided to seek financing for the construction of an industrial plant where ASECo would build mobile homes. After discussions with Clarence Hamilton, the president of an underwriting firm, Harrelson approached the town of Frisco City, Alabama for financing.

Under Alabama law, a municipality may establish industrial development boards with authority to issue tax-exempt bonds.[2] The statutory scheme provides for the board to build an industrial facility with the bond issue proceeds

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[1] The Eleventh Circuit, in the en banc decision Bonner v. City of Prichard, 661 F.2d 1206, 1209 (11th Cir. 1981), adopted as precedent decisions of the former Fifth Circuit rendered prior to October 1, 1981.

[2] See generally Ala. Code §§ 11-54-80 to -123 (1975).

and then to lease the facility to a commercial enterprise. The rent from the commercial enterprise is calculated to amortize the interest and principal of the bonds. The bonds are not general obligation bonds of the municipality, and the municipality is not liable for the payment of the industrial development board's obligations. Bondholders must look to the rental payments for satisfaction of their obligations. The bonds must be secured by a pledge of the commercial enterprise's revenues and may be secured further by a mortgage covering the plant.

Frisco City agreed to the establishment of an industrial development board for the financing of ASECo's mobile home facility. The development board signed a lease with ASECo on November 1, 1972, requiring ASECo to pay as rent the amount necessary to amortize the interest and principal of the bonds that the board would issue. Hamilton retained appellee Jerald Sklar, a Tennessee attorney, as bond counsel. Sklar drafted the lease, bond indenture, mortgage, and closing papers. Sklar also drafted the offering circular for the bond issue, which allegedly contained numerous material misrepresentations and omitted mate-

rial facts concerning the financial solvency and responsibility of Hamilton, Harrelson, and ASECo. The Phenix National Bank acted as trustee of the bond proceeds.

The bonds went on sale in three increments during 1972 and 1973. In January 1973, Tom Monks, the president of a Birmingham securities firm, advised his client Clarence Bishop that the tax-free industrial development bonds were a good investment opportunity. Monks told Bishop that others in the community had purchased the bonds. Bishop purchased three of the bonds in January 1973 for a total of $3,052.67, and one bond in February 1973 for $1,043.37. Bishop never read the offering circular and indeed never knew that one existed.

ASECo made two rent payments to the bond trustee; the trustee in turn made the first two interest payments to the bondholders. In April 1974, ASECo defaulted, and Phenix National Bank failed to make the third interest payment. The bank compiled a list of the names and addresses of persons holding the bonds at that time. After receiving the consent of 70% of all known bondholders, the bank foreclosed and sold the ASECo facilities. Eventually

the bank paid 37% of the face amount of the bonds to the 131 known bondholders.

On May 16, 1975, Bishop filed suit against Hamilton, Sklar, Sklar's law firm, Phenix National Bank, and numerous others, alleging that the defendants violated, inter alia, section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and the Securities and Exchange Commission's Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5. During the course of discovery, it became apparent that Bishop never saw the offering circular for the bond issue but bought the bonds solely on his broker's oral representations that the bonds were a good investment. The defendants moved to dismiss Bishop's action, arguing that Bishop's admitted nonreliance on any of the statements in the offering circular precluded recovery under Rule 10b-5. See Dupuy v. Dupuy, 551 F.2d 1005, 1014 (5th Cir.) (plaintiff must prove reliance on defendant's misrepresentation to recover under 10b-5), cert. denied, 434 U.S. 911 (1977). The district court agreed and, treating the defendants' motion to dismiss as a motion for summary judgment, granted summary judgment against Bishop.

The former Fifth Circuit, sitting en banc, reversed. Shores I, 647 F.2d 462. In Shores I, the court adopted a version of the "fraud on the market" theory of recovery under Rule 10b-5, whereby the requisite element of reliance may be satisfied by proof that the plaintiff relied on the integrity of the market without a showing of direct reliance on specific misrepresentations by the defendants.[3] Shores I involved an alleged fraud on the "undeveloped market," in that Bishop asserted that the newly issued Frisco City bonds were not entitled to be placed on the market at all and would not have been marketed but for the defendant's fraud. Under the theory of fraud on the undeveloped market approved in Shores I, the element of reliance is presumed once the plaintiff proves that the deception was material, i.e., that absent the deception the bonds would not have been marketed. See Ross v. Bank South, N.A., 837 F.2d 980, 995

[3] The classic version of the "fraud on the market" theory, known as "fraud on the open market," was first adopted by the Ninth Circuit in Blackie v. Barrack, 524 F.2d 891 (9th Cir. 1975), cert. denied, 429 U.S. 816 (1976), and was approved by this court in Lipton v. Documation, Inc., 734 F.2d 740 (11th Cir. 1984), cert. denied, 469 U.S. 1132 (1985). The Supreme Court expressly approved the "fraud on the open market" theory of recovery in Basic, Inc. v. Levinson, 108 S.Ct. 978 (1988).

(11th Cir. 1988).

The appellants petitioned the Supreme Court for a writ of certiorari, which was denied. Sklar v. Shores, 459 U.S. 1102 (1983). After the case returned to the district court, the named plaintiff (by then James Shores, the executor of Bishop's estate), moved for certification of a class action. Pending a ruling on the class certification motion, Norman Habshey moved for permissive intervention as a named plaintiff.

Following evidentiary hearings on both motions in August and September 1985, the district court denied both Shores' motion for class certification and Habshey's motion for intervention in a memorandum opinion issued July 30, 1985.[4] The court found that Shores had failed to prove (a) the existence of a class, (b) that the class was so numerous that joinder of all members was impracticable, (c) that Shores' claims or defenses were typical of the claims and

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[4] After the district judge to whom the case was originally assigned discovered that the brokerage firm handling his wife's investments had purchased shares for her in the holding company that owned Phenix National Bank, the judge recused himself, and the case was assigned to another district judge.

defenses of the class, or (d) that Shores would adequately protect the interests of the class.[5] As to Habshey, the court concluded that the motion to intervene was untimely. In addition, the court found that Habshey would not be an appropriate class representative because Habshey lacked even the most basic understanding of the claims and parties involved in the suit, Habshey's testimony lacked credibility, and Habshey's claims or defenses were not typical of the claims or defenses of the class.

Neither Habshey nor Shores immediately appealed the district court's order. Shores' individual action was assigned for trial in January 1987. On November 25, 1986, most of the defendants filed an offer of judgment to Shores in the amount of $20,600 pursuant to Fed. R. Civ. P. 68.

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[5] Fed. R. Civ. P. 23(a) provides that one may sue as representative of a class only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class. Courts have recognized that these requirements often overlap. See, e.g., General Telephone Co. v. Falcon, 457 U.S. 147, 157 n.13 (1982) (typicality and commonality); Eisenberg v. Gagnon, 766 F.2d 770 (3d Cir.) (typicality and adequacy), cert. denied, 474 U.S. 946 (1985); see also 3B Moore's Federal Practice q 23.06-2 (1987) (same).

Shores accepted this offer, and final judgment for $20,600, plus costs, was entered in favor of Shores on November 29, 1986.

On December 22, 1986, Shores filed a notice of appeal from the order denying class certification. In the same document, Habshey filed a notice of appeal from the order denying his motion to intervene. In this court, appellees moved to dismiss both appeals for lack of jurisdiction, arguing that Habshey's appeal was untimely and that Shores' acceptance of the offer of judgment eliminated the case or controversy necessary for article III jurisdiction. Appellees also oppose both appeals on the merits. We turn first to the jurisdictional issues raised by appellees.

II.

A.

A motions panel denied appellees' motion to dismiss Shores' appeal, citing Love v. Turlington, 733 F.2d 1562 (11th Cir. 1984). Under the rules of this court, the decision of the motions panel is not binding on the panel to which the case is assigned on the merits, 11th Cir. R. 271(f), and because of

the importance of the issue we consider it anew.

Appellees correctly state the general rule that a party may not appeal a judgment to which it has consented, absent an allegation of fraud, lack of actual consent, or failure of subject matter jurisdiction. See Swift & Co. v. United States, 276 U.S. 311, 314 (1928); Dorse v. Arstrong World Industries Inc., 798 F.2d 1372, 1375 (llth Cir. 1986). Appellees further note that a party may appeal from a judgment to which it has consented if that party expressly reserved its right to appeal. Dorse, 798 F.2d at 1376. In this case, Shores did not expressly reserve his right to appeal from the final judgment entered by the district court. Therefore, appellees argue, Shores may not appeal from that judgment.

Swift & Co. and Dorse do not tell the whole story, however. In a line of cases beginning with Deposit Guaranty National Bank v. Roper, 445 U.S. 326 (1980), the Supreme Court and this court have held that a named plaintiff may, after final judgment, appeal a district court order denying class certification even in some circumstances where the named plaintiff might be unable to appeal the final judg-

ment itself. In Deposit Guaranty, the Supreme Court held that named plaintiffs suing a bank on behalf of a class of credit card holders could appeal an order denying class certification even though the district court had entered, over the plaintiffs' objection, final judgment in each plaintiff's favor in the maximum amount that each plaintiff could have recovered. Noting that the named plaintiffs retained an interest in shifting the costs of litigation to the entire class, the Court reasoned that the plaintiffs retained a sufficient personal stake in class certification to support article III jurisdiction on the appeal from the order denying certification. Id. at 333, 338.

In United States Parole Commission v. Geraghty, 445 U.S. 388 (1980), decided the same day as Deposit Guaranty, the Supreme Court held that a named plaintiff could appeal an order denying class certification, even though the individual claim of the named plaintiff, a prisoner, had expired after the entry of final judgment due to his release from prison. Emphasizing the "flexible character of the Art. III mootness doctrine," id. at 400, the Court stated that "[a] plaintiff who brings a class action presents two

separate issues for judicial resolution. One is the claim on the merits; the other is the claim that he is entitled to represent a class." Id. at 402. Although the right to represent a class in some senses did not resemble the "personal stake" necessary for article III jurisdiction, nonetheless the controversy over class certification satisfied the essential values of article III jurisdiction—vigorous litigation and a concrete factual setting. The Court thus held that a proposed class representative retains a sufficient personal stake in the certification decision to appeal the denial of certification even after his own claim on the merits has expired. Id. at 404.

In Geraghty, the Supreme Court left open whether a plaintiff who settles its individual claim after denial of class certification may appeal the adverse ruling. Id. at 404 n.10. This court encountered precisely that situation in Love v. Turlington, 733 F.2d 1562 (11th Cir. 1984). The district court had denied the plaintiff's motion for class certification, and the parties had subsequently settled the case. Finding "no meaningful distinction between the settlement of the claim here at issue and the expiration of the claim in Geraghty,"

this court held that the class ratification issue continued to be a dispute capable of judicial resolution on appeal. Id. at 1565.

Appellees seek to distinguish Love by arguing that in that case the plaintiff expressly reserved her right to appeal; therefore Love was merely an application of the Dorse doctrine holding jurisdiction to exist when a party expressly reserves the right to appeal from an order to which it has consented. We cannot agree that Love will bear this interpretation. It is true that in Love the defendants expressly agreed not to contest the appealability of the certification order. The Love panel considered this agreement irrelevant to the jurisdictional inquiry, however, due to the established principle that federal subject matter jurisdiction cannot be created by agreement of the parties. Id. at 1564. Love relied explicitly and exclusively on the analogy to Geraghty to conclude that article III jurisdiction existed. Because Love squarely controls this case, we conclude that we have jurisdiction over Shores' appeal.

B.

We agree with appellees that we lack jurisdiction over

Habshey's appeal, however. The district court denied Habshey's motion to intervene on July 30, 1986. Although denials of motions to intervene are ordinarily immediately appealable, Brotherhood of Railroad Trainmen v. Baltimore & Ohio Railroad Co., 331 U.S. 519 (1947), Habshey waited 145 days after the denial of his motion to file a notice of appeal. Under 28 U.S.C. § 2107 and Fed. R. App. P. 4(a), a notice of appeal in a civil case must be filed within 30 days of the entry of the order from which the appeal is taken. This 30-day time limit is "mandatory and jurisdictional." Browder v. Director Department of Corrections, 434 U.S. 257, 264 (1978).

Habshey seeks to distinguish Railroad Trainmen by relying on Stringfellow v. Concerned Neighbors in Action, 107 S. Ct. 1177 (1987), in which the Supreme Court held that a party may not immediately appeal a district court's denial of its motion for intervention of right when the court simultaneously grants the party's motion for permissive intervention. Under the rationale of Stringfellow, such a movant becomes a party to an action when the trial court grants its motion for permissive intervention and can obtain

appellate review of the denial of its motion for intervention of right after final judgment. The would-be intervenors in Railroad Trainmen, by contrast, were not parties and could not appeal from the final judgment; thus they were entitled to appeal immediately the denial of their motion to intervene. Habshey likens himself to the intervenor in Stringfellow because he is a member of the putative class. He argues that because he was in some sense a party to the action, he could not have obtained immediate appellate review of the denial of his motion.

To accept Habshey's argument, we would have to conclude that Habshey, an unnamed member of a putative class, is a party who could obtain appellate review of a final judgment on the merits binding only the individual, named plaintiff. We need not delve into the jurisprudential complexities of precisely who is a "party" to a class action to conclude that Habshey's argument is without merit. In Guthrie v. Evans, 815 F.2d 626 (11th Cir. 1987), this court concluded that an unnamed member of a certified class has no standing to appeal a final judgment when the named plaintiffs have declined to do so. As we explained in Guthrie,

an unnamed member of a class action always has the option of moving to intervene in the course of the class action if he disagrees with the course of proceedings taken by the representative party. If the district court denies the motion to intervene, the unnamed class member may appeal that denial immediately. Id. at 628. Habshey has even a less meritorious position than did the appellant in Guthrie. If unnamed members of a certified class may not appeal from a final judgment on the merits but must move to intervene as named plaintiffs and appeal immediately if that motion is denied, it is even less likely that unnamed members of a putative class may wait until final judgment to appeal the denial of a motion to intervene. We therefore conclude that Habshey's appeal is untimely.[6]

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[6] Because we conclude that Habshey's appeal was untimely, we do not reach appellees' alternative argument that we lack jurisdiction over Habshey's appeal under this circuit's "anomalous rule," which precludes jurisdiction over an appeal from a district court's denial of a motion for permissive intervention unless the district court abused its discretion in denying that motion. See United States v. Jefferson County 720 F.2d 1511, 1515 (11th Cir. 1983).

III.

A.

Before addressing in detail the parties' contentions on the class certification issue, we summarize the reasons given by the district court for denying Shores' motion for certification.

First, the district court found that Shores had failed to identify the existence of a class.[7] In interpreting our mandate in Shores I that the district court "reconsider the maintainability of this action as a class action as to members of a properly defined class of Bond purchasers who did not . . . rely [on the offering circular]," 647 F.2d at 472, the district court believed that a certified class in this case could include only those bond purchasers who had not relied on the offering circular and must exclude bond purchasers who did so rely. With this understanding of the permissible class definition, the district court feared that extensive individ-

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[7] "By definition, an essential prerequisite to as class action is the existence of a 'class.'" 3B Moore's Federal Practice ¶ 23.04[1], at 23-98 (1987).

ual adjudication and fact finding would be necessary merely to determine which bond purchasers would be in the class.

Second, the district court found that Shores had failed to establish that the class was so numerous as to render joinder of all members impracticable. See Fed. R. Civ. P. 23(a)(1). In so concluding, the district court relied further on its understanding of our mandate in Shores I. Interpreting the class as limited solely to purchasers who did not rely on the circular, the district court found no evidence to suggest that such a class would be numerous. The district court also rejected the evidence proffered by Shores showing that the class of all bondholders was numerous, noting that under the doctrine of Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975), only purchasers or sellers of securities may state a claim under Rule 10b-5; mere holders of securities, as such, have no cause of action. In the district court's view, the numerosity of the class of bondholders had little, if any, relevance to the numerosity of the class of bond purchasers.

Third, the district court found that Shores had failed to establish that his claims or defenses were typical of the

claims or defenses of the class. See Fed. R. Civ. P. 23(a)(3). The court noted that Shores himself was not even a member of the class, as he personally had not purchased any bonds. Even in his capacity as executor of Bishop's estate, however, Shores presented atypical claims. Because both Bishop and Tom Monks (who sold Bishop the bonds) had died, significant difficulties of proof attended Shores' claim. No one, other than Bishop and Monks, could testify as to the circumstances of Bishop's purchase of the bonds. As a result, no one living could establish the truth of Bishop's allegations, that he had relied on the integrity of the undeveloped market in making his decision to purchase the bonds, and that he was willing to accept any marketable risk.

Fourth, the district court found that Shores was an inadequate class representative. See Fed. R. Civ. P. 23(a)(4). In support of this conclusion, the district court repeated its doubts that Shores would be able to establish the truth of Bishop's allegations. The court further determined that Shores' role as executor of Bishop's estate placed him in potential conflict with other members of the class, because Bishop's will placed Shores under an obligation to wind up

Bishop's affairs and distribute his assets within six months of Bishop's death. The district court also doubted whether Shores, as executor, would be willing to risk the estate's resources to pursue a small monetary claim.

B.

It is apparent that the district court's refusal to certify the class resulted largely from a misunderstanding of our opinion in Shores I. Unlike the district court, we have the benefit of two recent opinions of this court that have done much to clarify the meaning of Shores I and the scope of the "fraud on the market" theory generally. See Ross v. Bank South N.A., 837 F.2d 980 (11th Cir. 1988); Kirkpatrick v. J.C. Bradford & Co., 827 F.2d 718 (11th Cir. 1987), cert. denied, 56 U.S.L.W. 3643 (U.S. Mar. 21, 1988) (No. 87-835).

(1)

The district court was mistaken in its belief that the mandate of Shores I excluded from the permissible class any purchaser who had relied on the offering circular. As we

explained in Kirkpatrick, "the instruction that the district court determine the maintainability of a separate class for purchasers who did not rely was based simply upon the recognition that, as a practical matter, those purchasers should have a greater factual burden to establish liability than would those who relied on the offering circular. The instruction did not imply, however, that those who had relied on the offering circular could not also recover under the fraud-on-the market theory." 827 F.2d at 724 n.4.

The district court thus should not have refused to certify the class because it could not identify the class of persons relying on the integrity of the market but not relying on the offering circular without extensive factfinding. The essential characteristic of the fraud-on-the-undeveloped-market theory is that it renders distinctions based on individual patterns of reliance unnecessary. Once the plaintiff establishes the materiality of the fraud, reliance on the integrity of the market "is presumed with respect to all purchasers of securities. It is common sense that purchasers do not ordinarily seek to purchase a loss in the form of a fraudulently marketed bond." Ross, 837 F.2d at 995.

(2)

The district court's conclusion that Shores had not established that the purported class was sufficiently numerous was also influenced by its mistaken belief that Shores could represent only the class of purchasers not relying on the circular. As explained above, the distinction between purchasers relying on the circular and purchasers not so relying was immaterial. Shores was required to demonstrate only that the class of purchasers was numerous. See Ross, 837 F.2d at 995 (reliance presumed with respect to all purchasers once materiality of fraud on the undeveloped market is established).

The district court further concluded that Shores had not even carried the burden of showing that the class of bond purchasers was numerous, as the evidence adduced demonstrated only that Phenix National Bank had refused payment of interest to over one hundred bondholders. Testimony at the evidentiary hearing established that the bond coupons presented to Phenix National Bank were bearer

coupons; the list of bondholders compiled by the bank did not demonstrate who the original purchasers were. Because only a purchaser or a seller of a security may state a claim under Rule 10b-5, Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975), many of the bondholders who were refused payment by the bank might not have had a claim under 10b-5.

We need not consider whether Shores is correct that certain successors in interest to purchasers come within the Blue Chip Stamps rule to conclude that the district court erred. The district court was unduly concerned that every single member of the putative class be able to state a claim under the Blue Chip Stamps rule. At the class certification hearing, Shores was not required to demonstrate that every member of the putative class was likely to prevail on the merits; nor was he required to show the exact number of persons in the class. Shores had to show merely that the class was so numerous that joinder of all members was impracticable.

We understand the district court's concern that bondholders are not equivalent to bond purchasers for the

purpose of stating a cause of action under Rule 10b-5, but this concern did not justify refusing to certify the class for two reasons. First, the problem of individual members' inability to demonstrate that they were purchasers can be resolved through separate proceedings, if necessary, limited to that issue. Cf. Eisenberg v. Gagnon, 766 F.2d 770, 786 (3d Cir.) (district court abused discretion by refusing to certify class merely because some members might not be able to show reliance), cert. denied, 474 U.S. 946 (1985); Baxter v. Savannah Sugar Refining Corp., 495 F.2d 437, 443-44 (5th Cir.) (in Title VII class action litigation, district court should first consider whether employer's practices injured class as a whole and thereafter determine whether particular employees were actually members of the class who suffered injury), cert. denied, 419 U.S. 1033 (1974). The district court also could have ordered further proceedings to decide whether to divide the class into pre-default purchasers and post-default purchasers, if such a division eventually appeared necessary. By introducing the Blue Chip Stamps issue into the class certification decision, the district court erroneously considered the likelihood that un-

named plaintiffs would prevail on the merits. Cf. Eisen v. Carlisle & Jacquelin, 417 U.S. 156, 177-78 (1974).

Second, although numerosity of bondholders is not identical to numerosity of purchasers, the two issues are not completely unrelated. As bond trustee, Phenix National Bank had received a large number of coupons for the first three scheduled interest payments. Phenix National Bank made the first interest payment in May 1973, only six months after brokers began to sell the bonds. The market in which these bonds were traded was undeveloped, and nothing suggested that ownership of the bonds was drastically deconcentrated during the six months before the first interest payment became due. On the facts of this case, a demonstration that the class of bondholders as of the first interest payment was numerous probably sufficed to establish that the class of purchasers was numerous as well.

(3)

The district court erred in refusing to certify the class on the ground that Shores could not prove Bishop's allega-

tions. As we noted in Kirkpatrick, 827 F.2d at 723, an assessment of a plaintiff's likelihood of success on the merits is an improper basis for deciding the propriety of class certification. Furthermore, Shores' inability to establish the circumstances surrounding Bishop's purchase of the bonds was immaterial in this case, for "[i]f plaintiffs employ a fraud on the market theory, individual issues of reliance virtually disappear." Ross, 837 F.2d at 994 (quoting Dekro v. Stern Bros. & Co., 540 F. Supp. 406, 417 (W.D. Mo. 1982)). Shores does not need to show the detailed circumstances of Bishop's purchase to demonstrate Bishop's reliance; "a prima facie showing of reliance is established in a Shores type case upon proof of a scheme to bring securities onto the market which were not entitled to be marketed." Ross, 837 F.2d at 994. "Once the plaintiff proves that the deception was material (i.e. without it, the bonds would not have been marketed), reliance on the integrity of the market is presumed." Id. at 995.

Nor should the district court have refused certification because Shores could not demonstrate that Bishop was willing to accept "any marketable risk." One need not have

been willing to accept any marketable risk to have a "typical" claim of fraud on the undeveloped market. In Ross, we rejected the view that Shores I limited recovery to plaintiffs who would accept "any marketable risk." Shores I "was intended to offer protection to the general investing public from frauds which cause otherwise unmarketable securities to be marketed. Whether or not the investor has relied on the offering circular she may assume that the bonds are at least entitled to be marketed." Ross, 837 F.2d at 997.[8]

(4)

Finally, the district court erred in refusing to certify the class because of what it perceived as potential for conflict

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[8] As we explained in Ross, although essentially any investor may rely on the fraud on the market theory, an investor who relies on that theory exclusively does so at considerable peril. In a fraud on the undeveloped market case, an investor must show that the securities would not have been marketed at all absent the fraud. See Ross, 837 F.2d at 997; Shores I, 647 F.2d at 470. "The investor who fails to read or otherwise rely on disclosure statements forfeits many otherwise available legal rights." Ross, 837 F.2d at 997. Nonetheless, "even the risk averse investor who fails to read disclosure statements to ensure that his purchases are safe is entitled to a bottom line reliance on *the marketability of issued bonds.*" *Id.*

between Shores' obligation to Bishop's estate and Shores' obligation to the class. We hesitate to upset the district court's determination on this issue, for questions concerning class certification are ordinarily left to the sound discretion of the district court, Griffin v. Carlin, 755 F.2d 1516, 1531 (llth Cir. 1985), but we cannot accept the district court's conclusion that Shores was an inadequate class representative.

"The adequate representation requirement involves questions of whether plaintiffs' counsel are qualified, experienced, and generally able to conduct the proposed litigation, and of whether plaintiffs have interests antagonistic to the rest of the class." Griffin, 755 F.2d at 1533. As another circuit has stated, "[t]he representative must have common interests with unnamed members of the class, and . . . it must appear that the representatives will vigorously prosecute the interests of the class through qualified counsel." Senter v. General Motors Corp., 532 F.2d 511, 525 (6th Cir.), cert. denied, 429 U.S. 870 (1976).

Under either formulation it is clear to us that Shores fulfills the adequacy requirement of Rule 23(a)(4). Certainly

Shores has, in common with unnamed members of the class of purchasers, a financial interest in recovering against appellees under 10b-5. There is no doubt that Shores and his counsel have prosecuted this case vigorously and competently on behalf of both Bishop's claim and the class claim. Nothing on the record suggests that Shores' obligation to distribute Bishop's property within six months has interfered even remotely with the prosecution of this suit. Nor, in the nine years between Bishop's death and the district court's order, did Bishop's heirs ever move to abandon the claim.

IV.

It is not without considerable hesitation that we reverse the district court's denial of class certification, for in doing so we resuscitate litigation that had shown promising signs of termination. We are compelled to do so, however, because the district court's order is essentially at odds with the current substantive law of the "fraud on the market" theory. Accordingly, the appeal of Norman Habshey is

DISMISSED, the order of the district court denying class certification is REVERSED, the final judgment of the district court is VACATED, and the case is REMANDED with instructions to certify the class and for further proceedings consistent with this opinion.[9]

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[9] We reject appellants' contention that we should remand with instructions to enter judgment for the class. We are aware of no authority holding that a defendant's offer of judgment to a named plaintiff made pursuant to Fed. R. Civ. P. 68 estops the defendant to deny liability to a putative class.

FAY, Circuit Judge, dissenting in part; concurring in part.

While agreeing that the appeal of Habshey (section IIB) must be dismissed, I respectfully dissent from the denial of the motion to dismiss the Shores appeal (section IIA). Love v. Turlington, 733 F.2d 1562 (llth Cir. 1984), simply does not say or stand for the proposition set forth by the majority.

In the settlement of Love's individual claim, the parties discussed the fact that the ruling denying class certification would be appealed and the defendants agreed not to contest such. Id. at 1564. As the text of the opinion explains, Love had two claims: (1) one on behalf of herself individually and (2) one on behalf of an alleged class. She settled the first but not the second.

Dorse v. Armstrong World Industries, Inc. 798 F.2d 1372 (llth Cir. 1986), likewise offers no guidance or controlling authority since our court specifically found that "[as to]he stipulation for judgment . . . expressly recognized Eagle-Picher's intent to appeal . . . [as to] the government contract defense . . ." 798 F.2d at 1376. Although the

majority cites Roper, no mention is made of the fact that in that case the judgment appealed was entered over the objection of the plaintiff/appellant. As noted by the majority, Geraghty does not address the question.

In this matter the defendants made an offer of judgment to Shores. Shores accepted the offer and judgment was entered. There was no attempt made by Shores to reserve any rights whatsoever concerning the alleged class action. Unlike Roper, Shores voluntarily accepted the offer of judgment. The case was over and closed!

As stated in Dorse, 798 F.2d at 1375:

> Where the parties have agreed to entry of an order or judgment without any reservation relevant to the issue sought to be appealed, one party may not later seek to upset the judgment, unless lack of "actual consent" or a failure of subject matter jurisdiction is alleged. (citations omitted)

In my opinion the ruling by the majority is directly contrary to the language and spirit of Fed. R. Civ. P. 68 and renders it a nullity.

Although I would not reach the other issues pre-

sented, I continue to be concerned about the "fraud on the market" theory, see Ross v. Bank South, N.A., 837 F.2d 980, 1009 (11th Cir. 1988) (Fay, J., concurring), and hope our court will consider it en banc.

I would dismiss both appeals.

APPENDIX I

SHORES v. SKLAR

James L. SHORES, Jr., Executor of the Estate of Clarence E. Bishop, Jr., on behalf of himself and all other persons who purchased First Mortgage 8% Revenue Bonds issued by the Industrial Board of the Town of Frisco City, Alabama, Plaintiff-Appellant,

v.

Jerald H. SKLAR, et al., Defendants-Appellees.

No. 86-7898.

United States Court of Appeals,
Eleventh Circuit.

Appeal from the United States District Court for the Northern District of Alabama, James Hughes Hancock, Judge.

ON PETITION FOR REHEARING AND
SUGGESTION FOR REHEARING
IN BANC

(Opinion May 10, 1988, 11th Cir.,
1988, 844 F.2d 1485)

Before RONEY, Chief Judge, TJOFLAT, HILL, FAY, KRAVITCH, JOHNSON, HATCHETT, ANDERSON, CLARK, EDMONDSON, and COX, Circuit Judges *.

BY THE COURT:

A member of this court in active service having requested a poll on the application for rehearing in banc and a majority of the judges in this court in active service having voted in favor of granting a rehearing in banc,

IT IS ORDERED that the above cause shall be reheard by this court in banc with oral argument during the week of October 17, 1988, on a date hereafter to be fixed. The clerk will specify a briefing schedule for the filing of in banc briefs. The previous panel's opinion is hereby VACATED.

*Judge Vance is recused and did not participate in this decision.

APPENDIX J

Securities Exchange Act of 1934, §10(b) Manipulative and Deceptive Devices:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(b) To use or employ, in connection with the purchase of sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

APPENDIX K

Securities and Exchange Commission Rules:

"Rule l0b-S Employment of Manipulative and Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange.

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

APPENDIX L

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

FILED
Nov 25 1986
UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ALABAMA
CHARLES T. CLIVER, CLERK

JAMES L. SHORES, JR. , as Executor of the Estate of Clarence E. Bishop, Jr.,	)	
Plaintiff,	)	Civil Action No.
v.	)	CV 75-H-618-S
JERALD H. SKLAR, et al.,	)	
Defendants.	)	

OFFER OF JUDGMENT

To: W. Eugene Rutledge, Esq.
Attorney for Plaintiff, James L. Shores, Jr.
Rutledge & Kelly
1300 Brown-Marx Building
Birmingham, Alabama 35203

Pursuant to Rule 68 of the Federal Rules of Civil Procedure, defendants (other than Wilhelm Peppler, Joseph Savage and the Estate of George Rakerd) hereby offer to allow judgment to be taken against them (with a dismissal with prejudice of the claims against Wilhelm Peppler, Joseph Savage and the Estate of George Rakerd) in

this action, in the amount of Twenty Thousand Six Hundred Dollars ($20.600). together with costs accrued to date. This offer of judgment is made for the purposes specified in Rule 68, and is not to be construed either as an admission that any defendant is liable in this action, or that plaintiff or his testator has suffered any damage. Plaintiff is hereby notified that should plaintiff obtain a judgment less favorable than the offer recited herein, defendants will move the Court to tax all subsequent costs against plaintiff, including but not limited to, court costs, witness fees, attorneys' fees, and any and all other costs permitted by Rule 68.

/s/ Crawford S. McGiveren, Jr.
On behalf of all defendants
other than Joseph Savage,
Wilhelm Peppler and the Estate
of George Rakerd

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing Offer of Judgment has been duly served upon the

following attorney of record by placing same in the United States mail, properly addressed and postage prepaid this the 21st day of November, 1986.

W. Eugene Rutledge, Esq.
Rutledge & Kelly
1300 Brown-Marx Building
Birmingham, AL 35203

/s/ Crawford S. McGiveren
Of Counsel

APPENDIX M

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

JAMES L. SHORES. JR., as Executor of the Estate of Clarence E. Bishop, Jr .,	)	
Plaintiff,	)	CIVIL ACTION NO. CV 75-H-618-S
V.	)	
JERALD H. SKLAR, et al .,	)	
Defendants.	)	

NOTICE OF ACCEPTANCE OF OFFER OF JUDGMENT

Comes now the plaintiff in the above-styled cause, James L. Shores, Jr., as Executor of the Estate of Clarence E. Bishop, Jr., and pursuant to Rule 68 of the Federal Rules of Civil Procedure, hereby serves written notice that the "Offer of Judgment", heretofore made by certain of the defendants is hereby accepted by the plaintiff.

/s/ W. Eugene Rutledge
W. Eugene Rutledge, Attorney for
James L. Shores, Jr., as
Executor of the Estate of
Clarence E. Bishop, Jr.

OF COUNSEL:
RUTLEDGE & KELLY, P. C.
1300 Brown Marx Tower
Birmingham, Alabama 35203
Telephone: (205) 322-8761

CERTIFICATE OF SERVICE

I do hereby certify that I have served the foregoing on Crawford S. McGivaren, Henry E. Simpson and Hobart McWhorter, by hand delivery, and all other counsel of record and parties pro se by placing same in the United States Mail, first class postage prepaid on this the 25th day of November, 1986 .

/s/ W. Eugene Rutledge
Of Counsel

E: 2596

APPENDIX N

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

GRANTED
2-11-87
GUIN, Judge

JAMES L. SHORES, JR., Plaintiffs,

vs.

JERALD H. SKLAR, ALLEN COX, JR., ROANE WARING, JR., ERICH W. JAMES, ROBERT L.COX, LOUIS F. ALLEN, and FRED L. WATSON, JR., a partnership engaged in practicing law as Waring, Cox, James, Sklar and Allen; et al., Defendants.

Civil Action

CV 75-G-618-S

ENTERED
Feb 13 1987
U.S. District Court
of Alabama
Charles T. Cliver, Clerk

MOTION FOR ORDER TO PERMIT
PAYMENT OF JUDGMENT INTO COURT

Come now defendants, Jerald H. Sklar, Jr., Allen Cox, Jr., Roane Waring, Jr., Robert L. Cox, Louis F. Allen, and Fred L. Watson, Jr., a partnership engaged in practicing law as Waring, Cox, James, Sklar and Allen; Capell, Howard, Knabe & Cobbs, P.C.; First Alabama Bank of Phenix City, N.A.; Cecil Lamberson; Jackson Municipals,

Inc.; and Asa Candler V, and move the Court to enter an Order that the payment of the proceeds of the judgment and costs herein may be made into Court and directing the Clerk of this Court to indicate on the records of this Court, upon receipt, that the judgment has been paid. Defendants would show unto the Court the following:

1. On November 25, 1986, this Court entered judgment in conformity with the Offer of Judgment made by certain defendants. Costs of court were subsequently taxed by the Clerk, the amount of which was modified by this Court's Order of January 7, 1987.

2. Defendants have tendered to plaintiff's attorney two checks, representing the amounts of the judgment and the judgment together with costs and interest.

3. Plaintiff's attorney has refused to accept payment of the judgment, and has suggested that defendants pay the money into court. A copy of plaintiff's attorney's most recent refusal, which attached copies of the prior correspondence is attached hereto as Exhibit A.

4. Defendants attempted to pay the amount of the judgment, costs and interest into court on February 5,

1987, and were informed that the Clerk would not receive payment without order of this Court.

5. Defendants are entitled to pay the amount due under the judgment and to obtain an acquittance therefor.

/s/ Crawford S. McGivaren, Jr.
Crawford S. McGivaren, Jr.

/s/ Larry B. Childs
Larry B. Childs

Attorneys for defendants, Jerald H. Sklar, Jr., Allen Cox, Jr., Roane Waring, Jr., Robert L. Cox, Louis F. Allen, and Fred L. Watson, Jr., a partnership engaged in practicing law as Waring, Cox, James Sklar and Allen

OF COUNSEL:

CABANISS, JOHNSTON, GARDNER,
DUMAS & O'NEAL
1900 First National-Southern
Natural Building
Birmingham, Alabama 35203
(205) 252-8800

/s/ Hobart A. McWhorter, Jr.
Hobart A. McWhorter, Jr.
Attorney for Capell,
Howard, Knabe & Cobbs, P.C.

OF COUNSEL:

BRADLEY, ARANT, ROSE & WHITE
1400 Park Place Tower
Birmingham, Alabama 35203
(205) 252-4500

/s/ Henry E. Simpson
Henry E. Simpson

Attorney for First Alabama
Bank of Phenix City, N.A.

OF COUNSEL:

LANGE, SIMPSON, ROBINSON
& SOMERVILLE
1700 First Alabama Bank Building
Birmingham, Alabama 35203
(205) 252-7700

/s/ James L. Richey
Frank M. Young, III

Attorneys for Cecil Lamberson
and Jackson Municipals, Inc.

OF COUNSEL:

HASKELL, SLAUGHTER & YOUNG
800 First National-Southern
Natural Building
Birmingham, Alabama 35203
(205) 251-1000

/s/ Susan Salonimer
Lee H. Zell

Attorneys for Asa Candler V

OF COUNSEL:

BERKOWITZ, LEFKOVITS, ISOM,
EDWARDS & KUSHNER
1100 Financial Center
Birmingham, Alabama 35203
(205) 328-0480

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing Motion for Order To Permit Payment of Judgment Into Court has been duly served upon the following attorneys of record by placing same in the United States mail, properly addressed and postage prepaid this the 10th of February, 1987:

W. Eugene Rutledge, Esq.
Rutledge & Kelly, P.C.
1300 Brown Marx Tower
Birmingham, Alabama 35203

George B. Azar, Esq.
Azar, Campbell & Azar
260 Washington Avenue
Montgomery, Alabama 36103

Selma N. Resha, Esq.
2737 Highland Avenue
Birmingham, Alabama 35205

Thomas E. Martin, Esq.
700 Fairfield Road, N.W.
Atlanta, Georgia 30327

Joseph R. Manning, Esq.
Morris & Manning
Suite 2100
The Peachtree Center Tower
230 Peachtree Street
Atlanta, Georgia 30303

/s/ Larry B. Childs
Larry B. Childs
Of Counsel

LAW OFFICES OF
RUTLEDGE & KELLY, P.C.
1300 BROWN MARX TOWER
2000 FIRST AVENUE NORTH
BIRMINGHAM, ALABAMA 35203

W. EUGENE RUTLEDGE
KAY S. KELLY
CLYDE E. RILEY
J. MICHAEL COOPER

(205) 322-8761

February 3, 1987

RECEIVED
Feb 3 1987
Cabaniss, Johnston, Gardner, Dumas & O'Neal

HAND DELIVERED

Crawford S. McGivaren, Jr., Esq.
1900 First National/Southern Natural Bldg.
Birmingham, Alabama 35203

RE: Shores v. Sklar
Case No. CV-75-G-618-S

Dear Crawford:

I am in receipt of your letter of January 30, 1987 enclosing a check for $22,429.82 drawn on your law firm and made payable to "W. Eugene Rutledge as attorney for James L. Shores, Jr." You state in your letter a request that, presumably because you have sent me this check, I satisfy the judgment previously entered in the United States District Court for the Northern District of Alabama, Case No. CV-75-G-618-S. You thoughtfully sent copies of this letter, though I do not know whether you sent a copy of the check, to a number of lawyers and to Mr. Charles Cliver, clerk of the above court.

You earlier sent me a letter, on December 29, 1986, enclosing your law firm check in the amount of $20,600.00, made payable to me in the same language as is the instant check. I returned that check in a letter dated December 31, 1986.

Exhibit A

I am sending you with this letter a copy of (1) your letter of January 30, 1987, (2) a copy of your letter of December 29, 1986, (3) a copy of the check enclosed in your letter of December 29, 1986, and (4) a copy of my letter of December 31, 1386, in the event you have misplaced same. I am also sending along a copy of this letter, a copy of the above attachments and a copy of the instant check to those persons to whom you sent copies of your letter of January 30, 1987, so that each of them will have a complete copy of the correspondence you have initiated in this matter.

I am returning your law firm check dated "1/30/87" referred to above.

I regret to advise you that I cannot comply with your request to satisfy "the judgment that was entered in this action." There are several reasons for this, but two that should suffice are that you have failed to comply with the prerequisites to such satisfaction established by Rule 5 of the local district court and, since this matter is now on appeal, the local rules of the district court do not apply.

However, even if you do succeed in forcing me to "satisfy" that judgment referred to in your January 30, 1987 letter, it will be my position that such "satisfaction" falls within the doctrine of such cases as "di Leo v. Greenfield and McGowan v. King.

I suggest that, if your real interest is in paying this judgment rather than trying to create a basis to attack the appeal of this case, you pay the money into court.

Very truly yours,

RUTLEDGE & KELLY, P.C.

/s/ W. Eugene Rutledge
W. Eugene Rutledge

WER/dh
C: 1667
Enclosures
cc: Charles Cliver, Clerk
Hobart McWhorter, Esq.
Henry Simpson, Esq.
Frank Young, Esq.
Susan Salonimer, Esq.

CABANISS, JOHNSTON, GARDNER
DUMAS & O'NEAL
1900 FIRST NATIONAL-SOUTHERN NATURAL BUILDING
BIRMINGHAM, ALABAMA 35203
(205) 252-8800

MOBILE OFFICE
2210 FIRST NATIONAL BANK BUILDING
MOBILE, ALABAMA 36602
(205) 433-6961

R. H. CABANISS, 1857-1936
FORNEY JOHNSTON, 1879-1965

January 30, 1987

BY HAND

Mr. W. Eugene Rutledge
Rutledge & Kelly, P.C.
1300 Brown Marx Tower
Birmingham, AL 35203

Re: Shores v. Sklar, Case No. CV-75-G-618-5

Dear Gene:

Enclosed is a check in the amount of $22,429.82. This sum represents the amount of the judgment ($20,600), costs of court ($1, 719 .10) and post judgment interest at the rate of 5. 77% from November 25, 1986, the date of judgment, to December 29, 1986, the date on which we originally tendered you a check in payment of the judgment. In accordance with local Rule 5 of the United States District Court for the Northern District of Alabama, we request that you satisfy the judgment that was entered in this action.

Very truly yours,

CABANISS, JOHNSON, GARDNER, DUMAS & O'NEAL

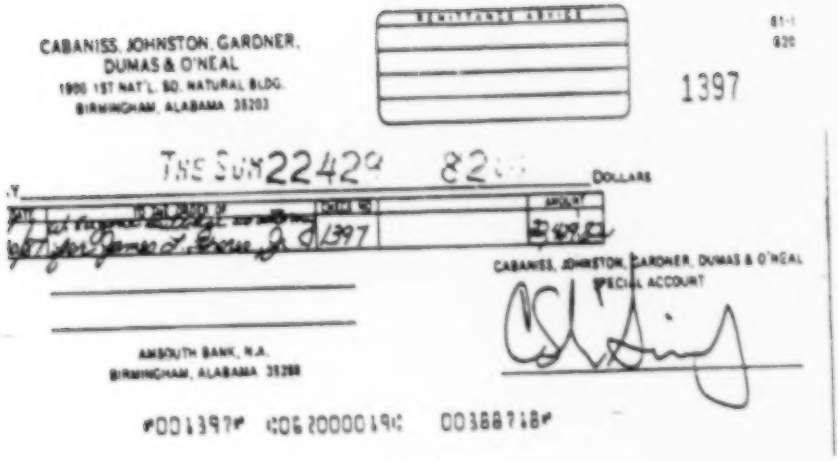
By:

/s/ Crawford. McGivaren, Jr.

CSMJr/bgr

Enclosure

cc: Charles Cliver, Clerk
Hobart McWhorter, Esq.
Henry Simpson, Esq.
Frank Young, Esq.
Susan Salonimer, Esq.



CABANISS, JOHNSTON, GARDNER,
DUMAS & O'NEAL
1900 1ST NAT'L. SO. NATURAL BLDG.
BIRMINGHAM, ALABAMA 35203

1397

THE SUM 2242[illegible] 82[illegible] DOLLARS

DATE	IN PAYMENT OF	NOTE NO.	AMOUNT
	[illegible]	1397	[illegible]

CABANISS, JOHNSTON, GARDNER, DUMAS & O'NEAL
SPECIAL ACCOUNT

AMSOUTH BANK, N.A.
BIRMINGHAM, ALABAMA 35288

#001397# C056000019C 00388718#

CABANISS, JOHNSTON, GARDNER
DUMAS & O'NEAL
1900 FIRST NATIONAL-SOUTHERN NATURAL BUILDING
BIRMINGHAM, ALABAMA 35203
(205) 252-8800

E.H. CABANISS, 1967-1936
FORNEY JOHNSTON, 1879-1965

MOBILE OFFICE
2210 FIRST NATIONAL BANK BUILDING
MOBILE, ALABAMA 36602
(205) 433-6961

December 29, 1987

Mr. W. Eugene Rutledge
Rutledge & Kelly, P.C.
1300 Brown Marx Tower
Birmingham, AL 35203

Re: Shores v. Sklar, Case No. CV-75-G-618-5

Dear Gene:

Enclosed is a check in the amount of $20,600 in payment of the judgment entered in this case. When the matter of costs is finally resolved by the Clerk of the Court, I will get you a check for that.

Very truly yours,

/s/ Crawford S. McGivaren, Jr.

/bgr

Enclosure

LAW OFFICES OF
RUTLEDGE & KELLY, P.C.
1300 BROWN MARX TOWER
2000 FIRST AVENUE NORTH
BIRMINGHAM, ALABAMA 35203

W. EUGENE RUTLEDGE
KAY B. KELLY
CLYDE E. RILEY
J. MICHAEL COOPER

(205) 322-8761

December 31, 1986

HAND DELIVERED

Crawford S. McGivaren, Jr.
CABANISS, JOHNSTON, GARDNER, DUMAS & O'NEAL
1900 First National-Southern Natural Building
Birmingham, Alabama 35203

RE: Shores v. Sklar
Case No. CV-75-G-618-S

Dear Crawford:

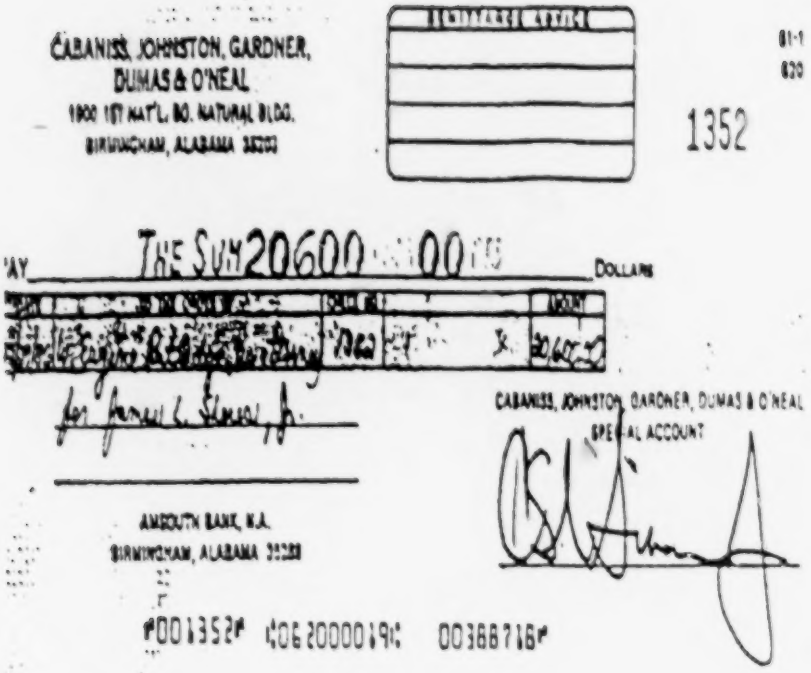
I am returning the enclosed check in the amount of $20,600.00 made payable to W. Eugene Rutledge, as attorney for James L. Shores, Jr. so that you may do with it as you think best in view of the pending appeal.

Best regards,

RUTLEDGE & KELLY, P.C.

/s/ W. Eugene Rutledge
W. Eugene Rutledge

WER/cl
C: 1617
Enclosure
cc: All Counsel of Record



CABANISS, JOHNSTON, GARDNER,
DUMAS & O'NEAL
1900 1ST NAT'L. BO. NATURAL BLDG.
BIRMINGHAM, ALABAMA 35203

81-1
620

1352

PAY THE SUM 20600 00 DOLLARS

for Russell L. Stewart, Jr.

CABANISS, JOHNSTON, GARDNER, DUMAS & O'NEAL
SPECIAL ACCOUNT

AMSOUTH BANK, N.A.
BIRMINGHAM, ALABAMA 35203

⑈001352⑈ ⑆062000191⑆ 00368716⑈